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ESTABLISH A BUILD AND CHARTER PROGRAM

COMPLETED

ORIGINAL

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HEARINGS

BEFORE THE

SUBCOMMITTEE ON MERCHANT MARINE

OF THE

COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST AND SECOND SESSIONS

ON

S. 1832 and S. 1833

TO AUTHORIZE THE ESTABLISHMENT OF A MERCHANT SHIP REVOLVING FUND, AND FOR OTHER PURPOSES

S. 1855

TO AUTHORIZE THE ESTABLISHMENT OF A MILITARY AUXILIARY REVOLVING FUND WITHIN THE TREASURY OF THE UNITED STATES, AND FOR OTHER PURPOSES

NOVEMBER 15, 1985 AND MARCH 20, 1986

Printed for the use of the
Committee on Commerce, Science, and Transportation

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ESTABLISH A BUILD AND CHARTER PROGRAM

FRIDAY, NOVEMBER 15, 1985

U.S. SENATE
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
SUBCOMMITTEE ON MERCHANT MARINE
Washington, D. C.

The subcommittee met, pursuant to notice, at 9:02 a.m. in room 253, Russell Senate Office Building, Hon. Ted Stevens, [chairman of the subcommittee] presiding.

Staff members assigned to these hearings: Bob Eisenbud and Brad Gilman, professional staff members; and John Hardy, minority staff counsel.

OPENING STATEMENT BY SENATOR STEVENS

Senator STEVENS. This subcommittee called this hearing to focus on the need for the creation of a build and charter program. The concept of build and charter is designed to increase the sealift capacity of the U.S. Armed Forces in a manner that promotes the U.S. shipbuilding industry.

In a nutshell, the concept directs the Navy to build commercially useful vessels in domestic shipyards and charter them to U.S. operators engaged in foreign commerce. The build and charter program originated in the Eisenhower Adminstration under the title of the Mariner program. That program called for the construction of 35 cargo ships which were known as Mariners. The vessels were constructed in U.S. shipyards. The majority were eventually sold to U.S.-flag shipowners.

The depressed state of the maritime and shipbuilding industries has forced Congress to review a variety of legislative proposals to increase competitiveness vis a vis foreign shippers and to assure a stable sealift capacity.

There is, as yet, no industry consensus on the best method of revitalizing the merchant marine.

Senator Inouye and I have met with the respresentatives of the maritime industry and discussed proposals which would fundamentally restructure Federal laws governing U.S. carriers engaged in operations between U.S. and foreign ports.

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The meeting illustrated that the industry remains divided about how to promote the U.S. merchant marine. The build and charter concept is something we should all be able to agree on, I believe.

There is an error, by the way, in the printing of the two bills. Both provide for entry into coastwide trade if the Secretary of the Navy finds it to be in the national interest. We did not reach a consensus on that point and that had been stricken from the bills prior to introduction, but the printers did not notice that the lines had been drawn through the draft. So that is an error in the original bill.

Let me make one comment here. I have a feeling that there still is not a consensus, either in the administration or in the industry, with regard to this program. This program dovetails with some $850 million that we have earmarked in the defense appropriations bill, to reprogram from prior years appropriations to deal with the Navy sealift problem.

In my judgment, if this program does not work, that money will not be available, and I certainly believe that it is one of the last opportunities we have to deal with sealift. Others will be remarking on it here today.

But as the chairman also of the Defense Appropriations Subcommittee, I find it very odd that the administration is willing to spend $100 million a year to tie up vessels that have no crew, have no management, but are apparently felt to be ready for emergency—and is unwilling to spend the money that is necessary to build new vessels that could be used in our foreign commerce and would be crewed and would be available with good management in the event of an emergency. I think that is our goal.

I hasten to point out that I am not provincial at all in this—no part of this bill will affect my State—and I am usually a very provincial Senator. But I think someone has to take a look at what is going on in terms of the merchant marine.

In the very near future, if we don't do something to stimulate the reconstruction and revitalization of our merchant marine, we will no longer be entitled to any role as a nation with merchant marine capability. That is particularly sad in the area of defense. I think this is the main thing that I would emphasize from point of view; the defense needs of our nation require a bill such as the one that is before us today.

I would like to emphasize the impact build and charter will have on our Nation's sealift capacity. The United States must be prepared to react quickly to global crises. The inadequacy of our Ready Reserve Fleet (RRF) reinforcxes the need to look for alternative sources of vessels. Build and charter presents a cost-effective augmentation of the RRF Program. Congress appropriates over $100 million annually to maintain vessels for the RRF. However, these ships require extensive work before they can be used to respond to emergencies. In addition, RRF vessels are not outfitted by experienceed crews. Build and charter would result in operational vessels crewed by experienced seamen. If administered properly, the long term costs of the program will be substantially reduced by the fees generated from chartering to private industry.

The fiscal year 1986 Defense Appropriations bill sets aside $852 million in prior-year savings accrued in the Navy's shipbuilding budget to be used as seed money for the creation of a build and charter program. This set asside is subject to the enactment of authorizing legislation. We are here today to review the merits of the concept of a build and charter program, and solicit comments on the form it should take should Congress endorse the program.

Senator Inouye.

Senator INOUYE. I would like to also emphasize the point that the Chairman has time and again brought to the attention of all of us here. In the event of an emergency, we do not have enough ships to supply our troops overseas for three weeks. And if that is adequate defense or adequate preparation, then I think we are in deep trouble.

We are trying our best not to just rebuild the merchant fleet, but to prepare our Defense Department in the event of some emergency overseas. I hope we will be prepared in the event of such an emergency.

Thank you very much.

[The bills follow:]

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99TH CONGRESS
1ST SESSION

S. 1832

To authorize the establishment of a Merchant Ship Revolving Fund, and for other purposes.

IN THE SENATE OF THE UNITED STATES

NOVEMBER 5 (legislative day, NOVEMBER 4), 1985

Mr. STEVENS introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To authorize the establishment of a Merchant Ship Revolving Fund, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Merchant Marine Act, 1936, as amended (46 App. U.S.C. 1141 et seq.), is amended by adding the following new title:

"TITLE XIV—BUILD AND CHARTER

"SEC. 1401. (a) There is established in the Treasury of the United States a fund, to be known as the 'Merchant Ship Revolving Fund' (hereinafter referred to as the 'Fund'). The Fund shall consist of—

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"(1) all moneys appropriated to the Fund;

"(2) all moneys received for the charter or sale of merchant vessels constructed under this section, except moneys from such charter or sale deposited in the Merchant Ship Working Capital Account established by paragraph (2) of this subsection;

"(3) any other moneys as may be made available for the purposes of the Fund.

"(b) The Fund shall be administered by the Secretary of the Navy (hereinafter referred to as the 'Secretary') and moneys in the Fund shall be used only for the construction, reconstruction or conversion in private shipyards in the United States of merchant vessels capable of serving as naval and military auxiliaries in time of war or national emergency.

"(c) The Secretary shall award contracts for the construction, reconstruction, or conversion of merchant vessels capable of serving as naval and military auxiliaries to private shipyards in accordance with the Federal Property and Administrative Services Act (41 U.S.C. 215 et seq.).

"(d) The Secretary shall charter to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in international commerce.

"(e) The Secretary may sell to a citizen of the United States for documentation under the laws of the United States

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any merchant vessel constructed under this section for operation in international commerce.

"(f)(1) The price the Secretary shall charge for the purchase [or charter] of a merchant vessel under subsections (d), (e), and (h) shall be not less than the cost the Secretary determines the purchaser would have incurred had the vessel been constructed outside the United States for delivery at the same time such vessel was delivered to the Secretary, taking into account financing terms and relative delivery times available from United States and foreign shipyards, less depreciation based on a twenty-five-year life of the vessel, and not including national defense design features and equipment.

"(2) The Secretary shall reduce the sale or charter price of a vessel constructed under this section to account for increased operating costs attributable to the addition of national defense design features and equipment.

"(g) In administering the first $850,000,000 appropriated to the Fund established by this section, the Secretary shall award construction contracts and charter or sell vessels constructed under this section subject to the restrictions set forth in paragraphs (1) through (4) of this subsection—

"(1) $130,000,000 of the Fund shall be allocated to the construction of vessels for charter or sale to persons who were parties to operating differential subsidy contracts for the operation of liner vessels under title

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VI of this Act on the date of enactment of this section, which persons received revenues in the year this section was enacted equal to or greater than $200,000,000 but less than $500,000,000, or shall be allocated to the construction, reconstruction or conversion of vessels under this section by or for the use of such a person.

"(2) $240,000,000 shall be allocated to the construction of vessels for charter or sale to any person who was a party to operating differential subsidy contracts for the operation of liner vessels under title VI of this Act on the date of enactment of this section, which person received revenues in the year this section was enacted of less than $200,000,000, or shall be allocated to the construction, reconstruction, or conversion of vessels under this section by or for the use of such person.

"(3) Any person acquiring or chartering a vessel for which funds have been allocated under this subsection may, as a credit against any payment required for such vessel, receive an amount equivalent to the value of a vessel or vessel offered by such person for inclusion in the National Defense Reserve Fleet or Ready Reserve Force. The credit shall be in the amount of

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the value of the vessel or vessels offered (determined in accordance with paragraph (4) of this subsection).

"(4) valuation provision.

"(h) The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the coastwise or intercoastal trade, except if the Secretary finds that it is in the interest of national security to so charter or sell any such vessel.

"(i) Within the Fund established by subsection (a), there is established an account, to be known as the 'Merchant Ship Working Capital Account' (hereinafter referred to as the 'Capital Account') in the amount of $15,000,000, which may be made available by the Secretary for the purpose of making working capital loans, on such terms and conditions as shall be established by the Secretary, to any person described in paragraph (g)(2). The Secretary may make such a working capital loan upon finding (A) that such loan is necessary to assist the applicant in completing a program of liner vessel acquisition or charter under this section and (B) that the applicant has suffered competitive harm from the enactment of legislation which allows the payment of operating differential subsidy or other compensation for the wage differential between United States and foreign crews without restriction as to the routes, lines or services served by vessels receiving

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subsidy. The authority provided in this subsection to establish a Capital Account shall terminate three years from the date of enactment of this section.

"(j) There is authorized to be appropriated to the Fund without fiscal year limitation such amounts as may be necessary to capitalize the Fund.".

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99TH CONGRESS
1ST SESSION

S. 1833

To authorize the establishment of a Merchant Ship Revolving Fund, and for other purposes.

IN THE SENATE OF THE UNITED STATES

NOVEMBER 5 (legislative day, NOVEMBER 4), 1985

Mr. STEVENS introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To authorize the establishment of a Merchant Ship Revolving Fund, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Merchant Marine Act, 1936, as amended (46 App. U.S.C. 1141 et seq.), is amended by adding the following new title:

"TITLE XIV—BUILD AND CHARTER

"SEC. 1401. (a) There is established in the Treasury of the United States a fund, to be known as the 'Merchant Ship Revolving Fund' (hereinafter referred to as the 'Fund'). The Fund shall consist of—

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"(1) all moneys appropriated to the Fund;

"(2) all moneys received for the charter or sale of merchant vessels constructed under this section; and

"(3) any other moneys as may be made available for the purposes of the Fund.

"(b) The Fund shall be administered by the Secretary of the Navy (hereinafter referred to as the 'Secretary') and moneys in the Fund shall be used only for the construction in private shipyards in the United States of merchant vessels capable of serving as naval and military auxiliaries in time of war or national emergency. For the purposes of this section, 'construction in private shipyards in the United States' means—

"(1) all major components of the hull and superstructure of the vessel are fabricated in the United States;

"(2) the vessel is assembled entirely in the United States; and

"(3) at least 50 per centum of the cost of all machinery (including propulsion) and components which are not an integral part of the hull or superstructure of the vessel relates to items procured in the United States.

"(c) The Secretary shall award contracts for the construction of merchant vessels capable of serving as naval and

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military auxiliaries to private shipyards in accordance with the Federal Property and Administrative Services Act (41 U.S.C. 251 et seq.).

"(d) The Secretary shall charter to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the foreign commerce of the United States after due advertisement and upon competitive bids.

"(e) The Secretary may sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the foreign commerce of the United States, either to the charterer of any such vessel under an option clause in the charter or, if the vessel is not under charter, after due advertisement and upon competitive bids.

"(f) The price the Secretary shall charge for the purchase of a merchant vessel under subsection (e) shall be not less than the cost the Secretary determines would have been necessary to construct the vessel, not including national defense design features and equipment, outside the United States for delivery to the Secretary at the same time such vessel was delivered to the Secretary less a reasonable depreciation, as determined by the Secretary based on a twenty-five-year life of the vessel.

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"(g) A citizen of the United States who charters or purchases from the Secretary any merchant vessel constructed under this section shall not be eligible to receive operating-differential subsidy under title VI of the Merchant Marine Act, 1936 (46 U.S.C. 1171 et seq.) for the operation of any such vessel.

"(h)(1) The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the transpacific or transatlantic general dry cargo service, except if the Secretary finds that any such vessel is—

"(A) required to replace an existing vessel or vessels under an operating-differential subsidy contract between the Secretary of Transportation and such citizen entered into pursuant to title VI of the Merchant Marine Act, 1936 (46 U.S.C. 1171 et seq.); or

"(B) necessary to replace an existing vessel or vessels twenty-five years of age or otherwise commercially obsolete.

"(2) The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the coastwise or intercoastal trade,

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except if the Secretary finds that it is in the interest of national security to so charter or sell any such vessel.

"(i) There is authorized to be appropriated to the Fund such amounts as may be necessary to capitalize the Fund.".

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99TH CONGRESS
1ST SESSION

S. 1885

To authorize the establishment of a Military Auxiliary Revolving Fund within the Treasury of the United States, and for other purposes.

IN THE SENATE OF THE UNITED STATES

NOVEMBER 23 (legislative day, NOVEMBER 18), 1985

Mr. STEVENS introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To authorize the establishment of a Military Auxiliary Revolving Fund within the Treasury of the United States, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Merchant Marine Act, 1936 (46 App. U.S.C. 1101 et. seq.), is amended by adding at the end thereof the following new title:

"TITLE XIV—BUILD AND CHARTER

"SEC. 1401. (a) There is established in the Treasury of the United States a fund, to be known as the Military Auxiliary Revolving Fund (hereinafter in this title referred to as the 'Fund'). The Fund shall consist of—

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"(1) all moneys appropriated to the Fund;

"(2) all moneys received for the charter or sale of merchant vessels constructed under this section;

"(3) all moneys received from repayment of construction differential subsidies awarded under title V of this Act; and

"(4) any other moneys as may be made available for the purposes of the Fund.

"(b)(1) The Fund shall be administered by the Secretary of the Navy (hereinafter in this title referred to as the 'Secretary'), in consultation with the Administrator of the Maritime Administration, and moneys in the Fund shall be used only for the construction in private shipyards in the United States of merchant vessels capable of serving as naval and military auxiliaries in time of war or national emergency.

"(2) For the purposes of this subsection, 'construction in private shipyards in the United States' means that—

"(A) all major components of the hull and superstructure of the vessel are fabricated in the United States;

"(B) the vessel is assembled entirely in the United States; and

"(C) at least 50 per centum of the cost of all machinery (including propulsion) and components which are not an integral part of the hull or superstructure of

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the vessel relates to items procured in the United States.

"(c) No contract for the construction of a vessel under this Act shall be made by the Secretary with any private shipbuilder, except after due advertisement and upon sealed competitive bids.

"SEC. 1402. (a) The Secretary may charter to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the foreign commerce of the United States after due advertisement and upon competitive bids.

"(b) The Secretary may sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the foreign commerce of the United States, either to the charterer of any such vessel under an option clause in the charter or, if the vessel is not under charter, after due advertisement and upon competitive bids.

"(c) The price of the Secretary shall charge for the purchase of a merchant vessel under subsection (b) of this section shall be not less than the cost the Secretary determines would have been necessary to construct the vessel, not including national defense design features and equipment, outside the United States for delivery to the Secretary at the same time such vessel was delivered to the Secretary less a

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reasonable depreciation, as determined by the Secretary based on a twenty-five year life of the vessel. The Secretary of Transportation shall recompute such estimated foreign cost annually unless, in the opinion of the Secretary, there has been a significant change in shipbuilding market conditions. The Secretary shall publish notice of an intention to compute or recompute such estimated foreign cost and shall give interested persons, including shipyards and shipowners and associations thereof, an opportunity to file written statements. The Secretary's consideration shall include all such relevant statements, and each determination shall include or be accompanied by a concise explanation of the basis of the determination.

"SEC. 1403. A citizen of the United States who charters or purchases from the Secretary any merchant vessel constructed under this section shall not be eligible to receive an operating differential subsidy under title VI of this Act for the operation of any such vessel.

"SEC. 1404. (a) The Secretary shall not charter the Department of the Navy's vessels to private operators except upon competitive sealed bids submitted in strict compliance with all the terms and conditions of a public advertisement soliciting such bids. Each advertisement for bids to construct, charter, or sell the Department of the Navy's vessels shall state the number, type, and militarily useful characteristics of

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the vessels the Secretary requires, the length of time for which the charter will be given, and all other information the Secretary considers necessary for the information of prospective bidders.

"(b) The Secretary may, and shall announce in any advertisements for bids that the Secretary reserves the right to, reject any and all bids submitted. All reasons for rejection of any bid, upon request of the bidder, shall be stated to such bidder in writing.

"SEC. 1405. (a) The Secretary shall award the charter to the bidder proposing to pay the highest monthly charter hire, unless the Secretary shall reject such bid for the reasons set forth in subsection (b) of this section.

"(b) In the warding of charters, the Secretary shall take into consideration the charterer's financial resources and credit standing, practical experience in the operation of vessels, and any other factors that would be considered by a prudent businessman in entering into a transaction involving a large investment of capital. All reasons for rejection of any bid, upon request of the bidder, shall be stated to such bidder in writing.

"(c) The Secretary—

"(1) may reject the bid if the charter hire is considered too low to replenish adequately the Fund; or

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"(2) may reject the bid if it is determined that the bidder appears to lack sufficient capital, credit, or experience to operate successfully the vessel over the period covered by the charter, and for any other reasons which would cause a prudent businessman to refrain from entering into a transaction involving a large investment of capital.

"(d) If the highest bid is rejected, the Secretary may award the charter to the next highest bidder, or may reject all bids and readvertise. All reasons for rejection of any bid, upon request of the bidder, shall be stated to such bidder in writing.

"(e) The Secretary may promulgate such regulations as are considered necessary for the purpose of implementing this section.

"SEC. 1406. (a) Every charter made by the Secretary pursuant to the provisions of this title shall provide that whenever, at the end of any calendar year subsequent to the execution of such charter, the cumulative net voyage profits (after payment of the charter hire reserved in the charter and payment of the charterer's fair and reasonable overhead expenses applicable to operation of the chartered vessels) exceeds 10 per centum per annum on the charter's capital necessarily employed in the business of such chartered vessels, the charterer shall pay over to the Secretary as additional

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charter hire one-half of such cumulative net voyage profit in excess of 10 per centum per annum, except that the cumulative net profit so accounted for shall not be included in any calculation of cumulative net profit in subsequent years.

"(b) Every charter shall contain a definition of the terms "net voyage profit" and "fair and reasonable overhead expenses," and "capital necessarily employed," as such terms are used in subsection (a) of this section, setting forth the formula for determining such profit and overhead expense and capital necessarily employed. Such definitions shall have been approved previously by the Secretary and published in the advertisement for bids for such charter.

"SEC. 1407. Every charterer of the Secretary of the Navy's vessels shall be required to deposit with the Secretary an undertaking with approved sureties as security for the faithful performance of all of the conditions of the charter, including indemnity against liens on the chartered vessels, in such amount as the Secretary shall require.

"SEC. 1408. Every charter shall provide that—

"(1) the charter shall carry on the chartered vessels, at its own expense, policies of insurance covering all marine and port risks, protection and indemnity risks, and all other hazards and liabilities, in such amounts, in such form, and in such insurance companies as the Secretary shall require and approve, ade-

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quate to cover all damages claimed against and losses sustained by the chartered vessels arising during the life of the charter, except that, in accordance with existing law, some or all of such insurance risks may be underwritten by the Secretary;

"(2) the charter shall at its own expense keep the chartered vessel in good state of repair and in efficient operating condition; and

"(3) whenever the President proclaims that the security of the national defense makes it advisable, or during any national emergency declared by proclamation of the President, the Secretary may terminate the charter without cost to the United States, upon such notice to the charterers as the President or Secretary shall determine.

The need for repairs under paragraph (2) of this section shall be based on the condition of the vessel immediately prior to the charter.

"SEC. 1409. (a) The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the trans-Pacific or trans-Atlantic general dry cargo liner service for a ten-year period after construction of such vessel is completed, unless the Secretary finds that any such vessel is—

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"(1) required to replace an existing vessel or vessels under an operating differential subsidy contract between the Secretary and such citizen entered into pursuant to title VI of this Act; or

"(2) necessary to replace an existing vessel or vessels twenty-five years of age or otherwise commercially obsolete.

"(b) The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the coastwise or intercoastal trade, unless the Secretary of Defense directs a waiver of compliance with this section to the extent considered necessary in the interest of national defense, after affording notice and an opportunity to be heard to existing coastwise or intercoastal trade operators.

"SEC. 1410. The Administrator of the Maritime Administration shall conduct a study of the program authorized in this Act and other promotional programs within the jurisdiction of the Maritime Administration to determine their potential application to the coastwise trades regulated under the Merchant Marine Act of 1920 (46 U.S.C. 861 et seq.). The study shall include a review of the costs of vessels engaged in the coastwise trade, and projections for the future cost of such vessels, and the differential between such vessels and

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those built in foreign shipyards. The Administrator shall submit the study to Congress by January 1, 1987.

"SEC. 1411. There is authorized to be appropriated to the Fund such amounts as may be necessary to capitalize the Fund.".

Senator STEVENS. This is going to be a hearing where there are a great many different entities involved, and we have established a series of panels. I am not going to turn on the lights. There is no reason to do that. It just irritates me and everybody else, too.

My feeling is that we should ask you to summarize your testimony and keep in mind that there are others behind you that would like to appear today. I think both Senator Inouye and I have other functions after the noon hour, so we could not continue this afternoon.

I would hope that you would agree to put your statements in the record to be printed in full, and summarize them for the benefit of those of us who are here at the hearing this morning.

Our first panel this morning is Everett Pyatt, Assistant Secretary for Shipbuilding and Logistics, Department of the Navy; and Mr. James Marquez, General Counsel, Department of Transportion, who is accompanied by Richard Bowman, the Associate Administrator for the Maritime Aids, Maritime Administration.

Mr. Pyatt.

STATEMENTS OF EVERETT PYATT, ASSISTANT SECRETARY, SHIPBUILDING AND LOGISTICS, DEPARTMENT OF THE NAVY; AND JAMES J. MARQUEZ, GENERAL COUNSEL, DEPARTMENT OF TRANSPORTATION; ACCOMPANIED BY RICHARD E. BOWMAN, ASSOCIATE ADMINISTRATOR FOR MARITIME AIDS, MARITIME ADMINISTRATION

Mr. PYATT. I would like to just briefly summarize my statement. Basically we are opposed to both bills. We believe that for such vessels to be commercially viable in international trade, the charter hire or sale price to the Government would have to be extremely low, perhaps only a token amount.

This would mean that the revolving fund would stand little chance of self-replenishment and would not be a viable long-term program to rebuild the U.S. merchant marine. Indeed, the program could take the nature of a direct subsidy.

S. 1832 also calls for allocation of build and charter ships to operators currently holding operating subsidy contract on the basis of revenues. We believe this to be inconsistent with the principle that competition for government contracts should be free and open.

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We share your desires for a strong and healthy merchant marine. And in Navy activities, we have tried to do what we could in our world to do that. We would like to continue working with you to that end.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR STEVENS AND THE ANSWERS

Question. I believe it is accurate to say that U.S. manufacturers and U.S. shipyards do not have the capability to build slow speed diesel propulsion systems. In the event of a conflict, would the lack of this capability cause problems if a merchant vessel needed repairs in a U.S. yard?

Answer. U.S. manufacturers have not chosen to make the initial investment and long-term commitment to slow-speed diesel manufacture in the U.S.A

During a conflict, running repairs and servicing of diesel plants are normally carried out by the ship's engineers. This type of repair could also be accomplished in U.S. ship repair yards. If major restoration work, requiring proprietary technical data, were required, the specialized expertise, materials, and tooling would not be available in the U.S. for high quality repairs.

Question. I believe the Navy's priority list of preferred vessel type in descending order of importance is: Ro/Ro's; Heavy lift ships; Barge carrying ships; combination Ro/Ro's, either break-bulk or container; Clean product tankers; and Self-sustaining break-bulk ships.

Would the Navy find slow speed diesel ships militarily useful?

Answer. Yes. Although ships powered by slow-speed diesel engines are generally slower than steam turbine ships, for sealift, speeds in the range of 17 knots for dry cargo ships and 15–16 knots for clean product tankers are acceptable.

Question. If any application were made for the Secretary of the Navy to construct for charter or sale a full containership, a crude oil carrier, or a dry bulk vessel, would the Secretary go ahead and construct the vessel? In other words, which standard is controlling: The type of ship an operator needs in order to complete commercially; or That the vessel be militarily useful?

Answer. The military utility of the ship would be the controlling standard. Since the proposed Mariner program would be a Navy program, designed to place ships in the active commercial fleet which can serve as military and naval auxiliaries, this is appropriate.

Question. Do you know what the cost of the 1950 Mariner Program was?

Answer. According to a 1976 Maritime Administration paper on the 1950 Mariner Program, the total construction cost of 35 ships was $341.9 million. Twenty-nine of the ships were sold to private operators for $150.5 million. The Navy has no information on other costs of the program such as administration.

Question. Both S. 1832 and S. 1833 would permit the Secretary of the Navy to waive the Jones Act prohibition in the bills, "if he finds it is in the interest of national security to so charter or sell any such vessel." Does the Secretary of the Navy now have such authority with respect to CDS or foreign-built, U.S.-flag vessels? If not, isn't this provision a further encroachment on the Jones Act?

Answer. The Secretary of the Navy has no such authority with respect to CDS or foreign-built, U.S.-flag vessels. The Secretary of the Navy does not administer the maritime aids programs that pertain to those vessels. Waiver of the Jones Act in the interest of national defense is not without precedent. Such waivers have been granted a number of times under the provisions of Public Law 891 (64 Stat. 1120) of December 27, 1950.

Question. In the event these vessels are allowed into the Jones Act trades, wouldn't the "playing field" be "uneven" vis-a-vis other Jones Act operators?

Answer. We believe that the Secretary of the Navy would exercise extreme care and judgment when deciding to allow these vessels into domestic trade. Sale price or charter rates should reflect such judgment.

Question. If the Secretary of the Navy "finds" that it is in the "interest of national security" to sell one of these vessels to a Jones Act operator, could the Secretary's "finding" be challenged in the courts?

Answer. The United States system of jurisprudence allows the legal challenge of virtually any statute. Such challenges are particularly common in maritime law.

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Mr. MARQUEZ. Thank you, Mr. Chairman. As you mentioned, Mr. Bowman is here with me today. I will not go through all of my formal statement which summarizes the bills, since everyone is pretty much familiar with them.

First of all, let me say that we at the Department do appreciate your efforts to support the U.S.-flag merchant marine. However, in this particular situation, we do not agree that build and charter is the correct approach, and therefore we oppose S. 1832 and S. 1833.

Of course, we view that enactment of our legislative proposals which were submitted in July and sponsored by you as S. 1481 and S. 1482 are the appropriate approach. As you know, those bills would authorize subsidized U.S.-flag operators to construct, reconstruct, or acquire vessels outside of the United States with immediate eligibility to participate in certain promotional programs.

Of the two approaches, the Department of Transportation supports the approach taken by S. 1481 and S. 1482 because it is consistent with administration policy that the expense of a modern commercial fleet should be borne by the private sector and not by the taxpayer.

In contrast, we believe that under the build and charter or sale programs outlined in S. 1832 and S. 1833, the purchase price or charter hire would have to be so low, in order to be commercially viable, that it would require annual appropriations in addition to the $850 million proposed in 1986 in order to continue the program.

Now, we are also in accord with the goals of a strong and healthy U.S. merchant marine and shipbuilding industry, but for some of the reasons articulated by the Navy, we concur in their position on S. 1832 and S. 1833.

That concludes my prepared statement, and we are available for questions if you have any.

[The statement follows:]

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STATEMENT OF JIM J. MARQUEZ, GENERAL COUNSEL, DEPARTMENT OF TRANSPORTATION

Mr. Chairman and Members of the Subcommittee on Merchant Marine. My name is Jim J. Marquez, and I am the General Counsel of the Department of Transportation. I am accompanied this morning by Richard E. Bowman, Associate Administrator for Maritime Aids of the Maritime Administration.

I am pleased to appear this morning to present the views of the Department with respect to S. 1832 and S. 1833, bills "To authorize the establishment of a Merchant Ship Revolving Fund, and for other purposes."

Both bills would amend the Merchant Marine act, 1936, by the addition of a Title XIV providing for a new Build and Charter or Sale Program. Pursuant to this program, the Secretary of the Navy would generally be authorized to construct in privately owned U.S. shipyards militarily useful merchant vessels, and sell or charter such vessels for operation under the U.S.-flag in the foreign commerce of the United States. The sale price would be calculated as if these vessels were constructed in a lower cost foreign shipyard. S. 1832 would apparently set the charter hire rate based on foreign construction cost. S. 1833 is silent on the charter hire rate.

Funds for the build and charter program would be provided by a Merchant Ship Revolving Fund (Fund) established in the U.S. Treasury, and administered by the Secretary of the Navy. Both bills would authorize appropriations to capitalize the Fund. The Fund would consist of:

Appropriated monies. Initially, we understand $852.3 million from unobligated prior year Defense shipbuilding appropriations would be used for this purpose;

Monies received from the sale or charter of merchant vessels constructed under the Program; and

Any other monies as may be made available for the purposes of the Fund.

Mr. Chairman and Members of the Subcommittee. The Department of Transportation deeply appreciates your continued efforts to support the U.S.-flag merchant marine. However, we do not agree that build and charter is the correct approach, and we therefore oppose S. 1832 and S. 1833. Instead, we view legislative proposals submitted by the Administration and introduced by the Chairman as S. 1481 and S. 1482 as the appropriate approach. As you know, pursuant to those bills, the Secretary of Transportation would authorize subsidized U.S.-flag operators to construct, reconstruct, or acquire vessels outside the United States with eligibility to participate in certain promotional programs.

Of the two legislative approaches, the Department of Transportation supports the approach taken by S. 1481 and S. 1482 because it is consistent with Administration policy that the expense of a modern commercial fleet should be borne by the private sector and not the taxpayer. In contrast, we believe that under the Build and Charter or Sale Program provided by S. 1832 and S. 1833, the purchase price or charter hire would have to be so low, in order to be commercially viable, that it would require annual appropriations, in addition to the $850 million proposed in 1986, in order to continue the program.

We are also in accord with the goals of a strong, healthy U.S. merchant marine and shipbuilding industry, but for the reasons articulated by the Navy, we concur in their position on 1832 and 1833.

Mr. Chairman. That concludes my prepared statement. I will be pleased to answer any questions that you or the Members of the Subcommittee may have. Thank you.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR STEVENS AND THE ANSWERS

Question. Doesn't allowing U.S. operators to build foreign and receive ODS, as the Administration's proposal would do, put non-subsidized U.S. carriers at a competitive disadvantage?

Answer. We do not believe that allowing subsidized U.S.-flag operators to construct or acquire vessels outside the United States and receive operating-differential subsidies for those vessels would place non-subsidized U.S.-flag operators in an unfair competitive position, because the vessels would replace existing vessels. Where any such foreign-built vessel is intended to be in addition to the existing service provided by an operator, before it could be placed in an essential service, subsection 605(c) of the Merchant Marine Act of 1936 requires that the Secretary make a determination that existing service is inadequate and that such additional capacity would further the purposes and policy of the Act.

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Question. The U.S. liner trades in the transpacific and the transatlantic are overtonnaged, and rates are depressed. In previous times we have seen that overtonnaging begat rebating, etc. Yet, despite overtonnaging, I think everyone would agree that our U.S.-flags do not carry a "substantial portion" of that cargo, as the Merchant Marine Act of 1936 mandates.

On the other hand, the Shipping Act mandates that our liner trades be open to everyone on a "come one, come all" basis.

My concern, therefore, is whether a "build and charter" program would exacerbate the overtonnaging problem; or, whether it might help U.S.-flag operators get a larger percentage of cargo in our international liner trades?

Answer. It is likely that new tonnage built under the programs established by S. 1832 or S. 1833 would be used to upgrade existing U.S.-flag fleets rather than to add new capacity to the currently overtonnaged containerized trade. This is for several reasons. First, the Navy preference would result in a program for the construction of Ro/Ro, LASH, and fast break bulk vessels. Also, because the U.S. general cargo fleet is relatively old compared to the foreign competitors and consists of obsolescent ships with steam power plants and large crews, there is an economic incentive to replace existing capacity rather than to simply add capacity. It follows that an operator with new, efficient replacement ships will have a greater ability to compete with the non-U.S.-flag carriers and perhaps gain a larger share of U.S. international trade. Finally, there may also be new markets for specialized vessels such as car carriers. In the areas in which the U.S. fleet does not compete at present, new U.S.-flag vessels will very likely increase U.S.-flag participation. However, it is the Administration's view that the correct approach to meeting the demand for replacement vessels as well as new tonnage is through build foreign authority, that has been introduced as S. 1481.

Question. Sea Land contends that the "playing field" would not be level if subsidized carriers were permitted to take advantage of the substantially lower cost of building foreign and retain ODS eligibility for those vessels.

To the extent that argument has merit, wouldn't it also apply to S. 1832, inasmuch as the bill uses the cost of building foreign as a guideline for the Secretary of the Navy in setting the charter or purchase price of vessels built under the bill; and allows the charterer or purchaser to trade in older vessels and offset the charter or purchase price by the value of the vessels traded in?

In other words, the charter rate or sale price would, in all probability, be based on the cost of a foreign-built vessel, less the value of the vessels traded in. Thus, a charterer or a purchaser on one of these vessels would be in an even better competitive position than an operator who built foreign and received ODS.

Answer. Due to uncertainties regarding the method of establishing the sale price under the program described by S. 1832 and the fact that the proposed legislation does not contain a provision determining the value of vessels to be traded in, it is impossible to say whether a vessel purchaser would be at an advantage. The payment of operating-differential subsidy is intended to support service on essential trade routes. It has no relation to where a ship is built other than the provision requiring that those ships that receive ODS be built in U.S. shipyards. When construction-differential subsidies were available, it was possible for an ODS recipient to acquire ships built in U.S. yards at a price comparable to foreign construction. If an ODS recipient were required to build replacement ships in the U.S. without CDS, the capital cost would be 2-3 times greater than a foreign-built vessel, thus creating a clear disadvantage for the ODS recipient.

Question. The suggestion has been made that any build and charter program should ensure that the most depressed shipyards get a fair share of such program's benefits.

Do you have any specific suggestions as to how this could be accomplished in legislation? I realize this is a difficult question, and you may want to submit your answer for the record at a later date.

Answer. We believe that directing contract awards to support a specific shipyard would constitute an unwarranted intrusion in the marketplace.

Question. I noted that the funds allocated under S. 1832 could be used to "construct vessels" for the account of the government, which vessels would than be chartered or sold to certain subsidized liner companies. Alternatively, the funds could be used for the "Construction, Reconstruction, or conversion" of vessels by or for the use of those same subsidized liner companies.

What is the difference between "constructing vessels" which are then to be "chartered or sold" and "constructing, reconstructing, or converting" vessels by or for the use of those same subsidized liner companies?

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Could the funds made available under S. 1832 be used to buy an old vessel from a subsidized operator, then reconstruct or convert it, and then charter or sell it back to that operator?

Answer. (a) We should point out that both bills are of a preliminary nature. The terms "reconstructing and converting" are not defined by the proposed legislation and it would be inappropriate to speculate as to the intended meaning of these terms.

(b) The legislation does not specify the source for vessels to be reconstructed or converted.

Question. Realistically, how many shipyards can expect to benefit from the build and charter programs in S. 1832 and S. 1833? Could we expect that such a program would save any shipyards that are now on the verge of shutting down?

Answer. We would expect normal market forces to operate in providing business for specific yards taking into account matters of series construction, operational considerations, and commercial needs. The initial amount of $850 million would provide sufficient funding to construct 8-10 ships. In the unlikely case that each ship were assigned to an individual yard a maximum of 10 yards might benefit. In the more likely case of series production of 2-5 ships of a type, 3-5 shipyards would be likely to benefit from the program.

It is possible that shipyards might temporarily ward off closure through such a program, but this cannot be stated conclusively.

Question. (a) Would any company other than Farrell, Waterman, or Prudential be eligible for a loan from the $15 million merchant ship working capital account in S. 1832?

(b) To be eligible for a loan from the merchant ship working capital account in S. 1832, the Secretary of the Navy would have to find that one of those operators had "suffered competitive harm from the enactment of legislation which allows the payment of operating-differential subsidy or other compensation for the wage differential between United States and foreign crews without restriction as to the routes, lines or services served by vessels receiving subsidy." In other words, Congress would have to enact legislation freeing ODS operators from their trade route restrictions, before a loan from the merchant ship working capital account could be made?

Answer. (a) The merchant ship working capital account would establish a fund of $15,000,000 to serve as the source of working capital for loans, to ODS recipients who received less than $200,000,000 in total revenue in the year of enactment of the legislation. In 1984, three currently existing ODS recipients accrued less than $200,000,000 is revenue: Farrell, Prudential and Waterman.

(b) Under the approach of S. 1832, Congress would have to enact additional legislation before a loan from the merchant ship working capital account could be made.

Senator STEVENS. Can you tell me, Mr. Pyatt, how many ships have we got in the Ready Reserve Fleet now, do you know?

Mr. PYATT. Approximately 60, in varied states of readiness ranging from 5 days to 30—to 20 days.

Senator STEVENS. Am I correct that they are unmanned? You don't have a manning crew assigned to them, do you?

Mr. PYATT. Most are not manned. Some have a skeleton crew that takes care of the ships in——

Senator STEVENS. That is maintenance.

Mr. PYATT.——in maintenance. Yes, sir.

Senator STEVENS. I stated that it cost about $100 million a year to keep those ships tied up; is that right?

Mr. PYATT. Your estimate is a little higher than mine, but it is approximately $1 million per ship per year.

Senator STEVENS. Do you have any management contract with anyone to put them to work for the Navy in the 5 days you are talking about?

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Mr. PYATT. For the ships that are on short recall notices, we do have, through MARAD, arrangements to crew the ships. It has been tested a couple of times and worked, but that is in a different situation than in the event of a national mobilization, I am sure.

Senator STEVENS. Are you familiar with the Mariner program at all?

Mr. PYATT. Over the last couple of years, I have spent some time studying it and getting acquainted with how it works and what happened to the ships. I have some knowledge, although it is not very intimate.

Senator STEVENS. At the time of the Mariner program, we had a substantial merchant marine.

Mr. PYATT. Yes, sir.

Senator STEVENS. But Eisenhower felt that we had to have a continuity as far as sealift was concerned, and brought the Mariner program into being. It was not continued beyond his administration.

There is no similar concept, is there?

Mr. PYATT. No, sir

Senator STEVENS. You don't have any vessels out there being manned, operated, and ready to turn to in the event the Navy needed them?

Mr. PYATT. The only vessels that are out there to do what you describe would be American-flag vessels which would come to our assistance, and this program would expend the number of American-flag vessels available for that end.

Senator STEVENS. And if they did that, that would exhaust our total commercial foreign commerce fleet. That would just be the Government seizing what was left of the merchant marine.

Mr. PYATT. Yes, because much of the merchant marine that serves the United States is currently foreign-flag, and the rest would be taken up from existing U.S. fleet. Yes, sir.

Senator STEVENS. As far as transportation is concerned, do you share the view of the need for increased sealift?

Mr. MARQUEZ. I am not sure that I can answer that question, Senator. I am not an expert in the area. Mr. Bowman may have some information that I don't. But I really cannot answer that question for you today. It is probably a better question for the Navy to answer.

Senator STEVENS. The administration's position appears to be that we should rely on the commercial sector to provide the sealift we need in the event of an emergency. Are they saying that since there is practically no commercial sector left that there is no need?

Mr. MARQUEZ. I don't believe the administration is saying that there is no need; no. I don't know what the military need is. I can't answer that for you, Senator. I am not sure what the sealift capability is. I do not have those facts at my command.

Senator STEVENS. Well, it is of no use to argue with you. I see the fine hand of OMB. When the times comes, we will argue with them.

Senator STEVENS. Senator Inouye.

Senator INOUYE. Thank you, Mr. Chairman.

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Mr. Pyatt, as the person in charge of logistics and shipbuilding for the Navy, do you really believe that a 60-ship reserve fleet is sufficient to meet the defense and strategic needs of the United States?

Mr. PYATT. No, sir. Our plans call for increasing the size of that to something over 100 ships for the reasons that you have outlined already. And we continually do a recalculation of what we need in the RRF, depending on what is happening in the U.S. merchant marine active fleet.

Clearly, more ships in the active fleet would mean that we would need less in the reserve fleet. But those ships in the active fleet would have to be militarily useful. Large container ships are less useful than other classes of ships, for example.

Senator INOUYE. What sort of ships are in your reserve?

Mr. PYATT. We are currently buying roll-on/roll-off ships; self-sustaining ships of the LASH category, and breakbulk ships. We would like to buy some smaller product tankers in the 35–50,000 ton range. These are the kinds of ships we believe are most militarily useful. Heavy lift ships capable of handling the heavy equipment that goes along with a military expedition—those are the kinds of ships we would be most interested in.

Senator INOUYE. Are these ships in operation?

Mr. PYATT. Some are in operation in the U.S.-flag fleet, and by virtue of their age and the changing economic conditions of the market, they are no longer economically useful, but they are militarily useful. And for this reason we have been trying to buy them.

Senator INOUYE. Of the 60, how many are now in use?

Mr. PYATT. Of the 60? None are currently in use, sir. They are all tied up.

Senator INOUYE. So our Chairman is trying to propose a program—and I must concur with him almost in desperation to assist our industry—that would permit the construction of ships and put them into operation.

Do you see anything wrong with that?

Mr. PYATT. From purely a military planning point of view, the ships that would be in operation and under U.S.-flag would be available for military use, and the Navy would not have to buy so many in the RRF.

The rest becomes an economic tradeoff of what is the best way to proceed. The broader policy issues I have outlined this morning in my testimony.

Senator INOUYE. How long will it take your reserve fleet to become operational?

Mr. PYATT. It varies. On the categories of ships—and I would like to submit more details for the record—I did not bring it with me—but it varies from 5 days to about 20 days. And then the ships in the NDRF that are not kept up so well are from 30 to 60 days.

Senator INOUYE. So we would have a fleet that can be operational anywhere from 5 to 60 days.

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Mr. PYATT. Yes, sir.

Senator INOUYE. Don't you prefer to have at least a portion of a fleet that could be ready in 24 hours?

Mr. PYATT. Well, I am not sure it would be ready in 24 hours, but a fleet that is manned and operating is clearly more nearly ready. And then you hope that when you want it, it is in the right location and not on the other side of the world.

But it is not a simple task to take a piece of cold steel and get it ready to run, and get crews there who know how to run it and run it well. It is a task that one cannot gloss over.

Senator INOUYE. Your position is very clear. You are opposed to both bills.

Does the Navy have any proposal to make to us?

Mr. PYATT. Our only proposal in looking at the choices that we had—and this is how we developed the plan for the Ready Reserve Fleet, for the expansion of the Ready Reserve Fleet—from our perspective and the alternatives that were available to us, the RRF was the preferable one.

Senator INOUYE. Finally, sir, do you believe it is in our national interest to have an active, viable merchant fleet?

Mr. PYATT. Yes, sir.

Senator INOUYE. But you don't believe that this program will bring this about?

Mr. PYATT. No. There are a lot of elements to it. You have to have people, and you have to have ships and you have to have business.

Senator INOUYE. Mr. Chairman, I have several questions that I have prepared that I would like to submit to both gentlemen.

Senator STEVENS. Fine. Thank you very much, Senator.

If we had this program of build and charter, what would the Navy like to see us buy?

Mr. PYATT. We would clearly be interested in tankers in the range of to 50,000 tons of product tankers to carry fuel; heavy lift ships; roll-/roll-off ships, self-sustaining container or breakbulk ships; combination ships. Those categories I think would be the ones we would be most interested in.

Senator STEVENS. Do you have those in this Ready Reserve Fleet now?

Mr. PYATT. We have several of each category, with the exception of heavy lift ships. We do not have a heavy lift ship in the Ready Reserve Fleet.

Senator STEVENS. I asked you the question about the crews. Do you examine into the adequacy of availability of trained people to man the Ready Reserve Fleet?

Mr. PYATT. It is clearly a problem from my perception, because to operate ships effectively people need to be active in ship operations. In the existing merchant marine, it is my understanding there are skilled people not fully employed right now. If they are not fully employed now, what happens in the long term? I think they would decline, and we would begin to have a manning problem.

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Senator STEVENS. Thank you very much, gentlemen. We appreciate you coming. We hope we can give you a new program whether you like it or not.

Senator STEVENS. The next group is the group of the subsidized liners: William Verdon, the vice president and general counsel, U.S. Lines, Inc.; Richard Tavrow, senior vice president, secretary, and general counsel, American President Lines; Hans Blocklin, senior vice president, Lykes Brothers Steamship Company; George Lowman, chairman of the board and chief executive officer, Farrell Lines, Inc.; and Spyros Skouras, Sr., president and chief executive officer, Prudential Lines, Inc.

Gentlemen, you have to decide what order you go in. If the order I read is agreeable to you, fine; otherwise you tell us who would like to go first.

STATEMENTS OF GEORGE F. LOWMAN, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, FARRELL LINES, INC.; WILLIAM P. VERDON, VICE PRESIDENT AND GENERAL COUNSEL, U.S. LINES, INC.; RICHARD L. TAVROW, SENIOR VICE PRESIDENT, SECRETARY, AND GENERAL COUNSEL, AMERICAN PRESIDENT LINES; HANS G. BLOCKLIN, SENIOR VICE PRESIDENT, LYKES BROTHERS STEAMSHIP COMPANY, INC.; AND SPYROS S. SKOURAS, SR., PRESIDENT AND CHIEF EXECUTIVE OFFICER, PRUDENTIAL LINES, INC.

Mr. LOWMAN. Mr. Chairman, I will make a presentation on behalf of all the subsidized carriers.

Senator STEVENS. Very well.

Mr. Chairman, Senator Inouye, and members of the committee, I am George Lowman, chairman and chief executive officer of Farrell Lines, Inc. I am appearing here today to comment on conditions in the U.S. maritime industry and related legislative matters on behalf of the following U.S.-flag liner operators: American President Lines, Inc., represented by Mr. Tavrow; Lykes Brothers Steamship, represented by Mr. Blocklin; Prudential Lines, Inc., represented by Mr. Skouras; and United States, represented by Mr. Verdon.

The operators for whom I speak would like to thank the Chairman and the Ranking Minority Member of this subcommitee for the time and effort which they have expended in informal working sessions trying to bring together the various factions within the merchant marine industry. The operators I represent are committed to working with this subcommittee to try to solve the problems which plague the entire industry, and thereby save a U.S.-flag fleet which, as the Chairman has previously so aptly observed, is in serious decline.

My remarks today will: (1) survey the needs of all sectors of the maritime industry, including the public sector; (2) set forth a prescription for a healthy merchant marine industry; (3) explain why a build and charter program in and of itself offers only an incomplete solution

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to the problems facing both public and private sectors of the merchant marine industry; and (4) urge this subcommittee to continue to work for an industry consensus to effect a complete solution.

With reference to the overall needs and in particular the public sector needs: As this subcommittee fully understands, but others may not, the merchant marine industry differs from most other industries in this country because it has both public and private missions. The public mission is to provide for a sealift capacity for the defense of the nation. An attached statement explains in detail the defense role which the U.S. Government expects the merchant marine industry to play.

The bottom line is this: the United States needs to maintain (1) financially viable U.S.-flag commercial operators which use up-to-date equipment and (2) which employ U.S. seamen able to man this equipment and thereby form the manpower base to activate the 70-odd ships in the Ready Reserve Fleet; and (3) it also needs to maintain a domestic shipbuilding capacity.

With regard to the private sector needs: Left to the diciplines of the marketplace, the United States merchant marine as we know it would have disappeared long ago. The services it performs can be performed cheaper by foreign entities, many of which are government-owned companies, and most of the remainder are themselves subsidized by their governments despite cheaper wages, fewer benefits and other employment conditions prevailing in their own countries.

The issue facing this subcommittee, the Congress and the administration is how the United States can continue to maintain U.S.-flag commercial operators which employ U.S. seamen and also maintain a domestic shipbuilding capacity.

The public needs require governmental participation in the merchant marine industry to some degree. The challenge is to maximize the opportunity for the disciplines of the marketplace to work while meeting the public needs.

The prescription or the medicine is fairly simple:

(1) Let the Defense Department maintain U.S. shipbuilding by undertaking a U.S. build and charter program which allows commercial operators to acquire U.S. ships at prices competitive with foreign prices.

(2) Let U.S.-flag liner operators acquire their ships in the world market and pay them wage differential subsidies to compensate them for the higher costs of using U.S. seamen and maintaining a U.S. sealift capacity.

(3) Let these liners compete in foreign trade unfettered by regulations.

Those three elements are what we describe in our paper as the prescription or the medicine. We will refer to it hereafter as the prescription.

Unfortunately, filling the prescription is very difficult. Historically, the prescription was filled by offering the subsidized commercial carriers wage and construction subsidies, but imposing upon them regulatory and other constraints to protect their unsubsized competitors. The wage differential program prohibited subsidized carriers from ac-

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quiring foreign-built ships, but construction subsidies permitted them to build in the U.S. yards at a capital cost in parity with foreign competitors.

This historical prescription is now threatening to kill the patient. In the past decade, U.S. commercial shipbuilding has lost ground to foreign competition from standpoints of costs, delivery time and technology. The 50 percent subsidy on U.S. construction obviously became inadequate when the costs of the U.S.-built ships became 300 percent more expensive.

In 1981 the subsidy funds dried up altogether, but to build foreign restrictions remained. Thus, subsidized commercial operators have been placed in a substantial disadvantage with respect to foreign competition and the public need for U.S.-flag commercial liner operators manned by U.S. crews is being threatened.

The Chairman and the ranking minority member of this committee have made efforts to obtain a consensus of the prescription set forth above. To date, attempts to compromise have not been successful. However, we will vigorously continue our efforts in the hope that the prescription outlined above can be filled.

With respect to the build and charter program: In the meantime this subcommittee has asked us to comment specifically on the build and charter program. Let us say at the outset that we favor a build and charter or similar program as one element of the prescription for a healthy U.S. merchant marine. We see no other way to maintain a U.S. commercial shipbuilding capacity at this time. We know we cannot buy U.S.-built ships at their current prices. We know that in terms of cost, financing, ddelivery times, and technology, U.S.-built ships can no longer compete. We also know that the U.S. shipbuilding capacity is an important public defense need for which the public should pay.

In short, we support the efforts of you, Mr. Chairman, and Senator Inouye and others, to bring to the table this very important part of the prescription for a healthy merchant marine. The form of the program is another matter. If the prescription is a correct one for the merchant marine, one that meets public needs through reliance upon an efficient private sector effort—and we believe it is—then the form of the build and charter program is not as important as its existence or the existence of a similar program.

Obviously, S. 1832 has been drafted in the context of more encompassing legislation and only makes sense in that context.

S. 1833 is another bill which, with significant modifications, could fill one element of the prescription. Of course, we would not want a program that permitted the market to be flooded with commercial vessels competing in dense markets with existing operators. Permitting foolhardy new entrants to put established liner operators out of business would destroy the public need for a long-term, financially viable commercial liner operation. The form of the build and charter program needs to be molded to fit the practical exigencies of the current situation in the merchant marine industry.

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We reiterate our strong support for S. 1481, the administration's build foreign program.

The dilemma for all of us who recognize the urgent need to move now to preserve a healthy merchant marine for our national defense is to endure the current wait without losing one important element of the current prescription—namely the build and charter program.

Recognizing the time constraints facing all of us, in the final analysis the only effort which makes sense to us is to try to fill the prescription for a healthy merchant marine in whole rather than in part—and to do it now. We urge all segments of the industry to join with us in working in public or private forums to develop a consensus position that meets the public needs of a military sealift capacity including: (1) Financially viable U.S.-flag liner operators operating vessels constructed in foreign yards, utilizing U.S. crews, and being paid wage differential assistance for such use; and (2) a viable shipbuilding capacity through some program such as build and charter program.

We stand ready to work with this subcommittee and any other parties to try to bring about this result.

Thank you very much.

[The attachment referred to follows:]

Our National Security Depends Upon a Modern Liner Fleet

The revitalization of our merchant fleet is essential not only for commercial reasons, but more importantly for security reasons. Our national defense strategy relies upon the U.S.-flag merchant marine to serve as the major component of this nation's sealift force in times of war or other national emergency. This strategy envisions the oceans as barriers in our defense and presupposes that a general war should be waged closer to the ememy's borders than to our own. It recognizes the fallacy of presuming that our next war will be short term. The Korean and Vietnam Wars, even though they occurred in the nuclear era, were wars of long duration. For a war or economic blockade of any significant duration, this country must rely on its cargo vessels.

There are no plans for a major overseas military operation which do not comtemplate the use of sealift. Two of our states, Alaska and Hawaii, and 40 of our 42 allies are overseas. We maintain military divisions in Hawaii, Germany, Korea and Japan. In a time of war or in the event of an OPEC-type blockade, our noncontiguous states, our overseas forces and the forces of our allies would need to be reinforced and resupplied. U.S.-based divisions required overseas would need to be transported. In a major conflict, 95% of all dry cargo and 99% of all petroleum products would travel by sea. The U.S. merchant marine would provide two-thirds of the U.S. flag portion of this massive sealift.

A. AIRLIFT CANNOT MEET THIS NEED

Airlift cannot substitute for sealift to deliver the massive quantities of materials needed for a modern war. The Military Sealift Command estimates that a single mechanized division would require more than 100,000 tons of cargo for deployment and more than 1,000 tons of cargo per day for sustained operation. Even the combination of the entire Defense Department strategic airlift and all available commercial aircraft in the Civil Reserve Air Fleet would only be able to deliver 2,500 tons of cargo to Southwest Asia per day. A single cargo ship of moderate capacity like a C-7, on the other hand, can carry 20,000 tons of cargo. It can also accommodate the bulldozers, bridges, tank retrievers, and the other organic equipment of modern armies which will not fit in most aircraft.

Sea transport also does not present the significant fueling problems that arise with air transport. Airlift consumes enormous quantities of fuel. In the 1973 Yom Kippur war, our airlift support of Israel required six tons of aviation fuel for every ton of military cargo delivered in Tel Aviv. Aviation fuel may also not be available at the far end of the cargo aircraft's supply line.

B. THE NEW MARINE TECHNOLOGY PROVIDES THE MOST EFFECTIVE TRANSPORT OF MILITARY SUPPLIES

The Navy has recognized the importance of sealift and furthermore has recognized the importanct of the newer automated container vessels. During the Vietnam War, the modern port at Cam Rahn Bay provided the most efficient transportation of military supplies. While the older breakbulk vessels may be useful in undeveloped ports, their slow rates of cargo loading and unloading create supply backups. The longer time lag in combat areas also subjects these vessels and their crews to greater damage and casualties. The more modern containerships not only reach their destinations sooner, but also, by utilizing specialized dockside facilities or auxiliary crane ships, greatly speed the cargo handling process. By delivering cargo in a form ready for disbursement to inland depots, they also prevent the unnecessary concentration of supplies at port areas.

To take full advantage of the advanced commercial technology, the Department of Defense has invested heavily in programs to adapt commercial vessels for special military uses through the use of specially designed pallets (flat racks), oversized containers (sea sheds) and mobile piers (elevated causeways). Auxiliary crane ships—containerships enhanced with movable cranes (T-ACS)—can load and unload their own cargo as well as that of other ships. The DOD is also attempting to adapt its ground forces equipment to containerization or to provide adaptors for the transport of this equipment on containerships.

C. ONLY THE PRIVATELY-OWNED U.S.-FLAG MERCHANT MARINE CAN MEET THE MILITARY'S VITAL SEALIFT NEEDS

Our national defense strategy relies upon the privately-owned U.S. flag merchant marine to provide the overwhelming bulk of our sealift capability and as the source

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of second-hand ships for government-owned fleets. Sealift sources other than the active U.S.-flag merchant marine can only supplement these needs.

The Military Sealift Command (MSC) includes just 6 Navy-owned specialized cargo ships. It relies on the merchant marine for the 26 privately owned U.S.-Flag liners presently on charter to the government. The National Defense Reserve Fleet (NDRF) includes 137 mothballed freighters. But due to their World War II vintage, heavy prior use and the lack of replacement parts, 107 of these are of questionable value. The Ready Reserve Force (RRF), which consists of vessels capable of being put to sea within five to ten days, includes 65 ships now, but will expand to 76 ships in 1985 and 97 ships in 1986. Vessels in the RRF have come almost exclusively from the U.S. merchant marine.

Crews for the reserve fleet—as well as many MSC vessels—would come from the pool of active merchant seamen. This pool exists, of course, only because the U.S. merchant marine generates the demand for civilian mariners.

An operational U.S.-flag fleet also has the advantages of reliability, cost-effectiveness, and readiness in comparison with a reserve or a foreign-flag fleet. An active vessel, unlike a reserve vessel, has an active, trained crew ready to serve immediately in an emergency.

Furthermore, U.S.-flag vessels crewed by 100% U.S. citizen crews do not raise the reliability concerns of vessels manned by foreign crews. The 1973 Mideast crises showed that our allies will not participate in unilateral U.S. military actions involving Arab or Moslem countries and that even U.S.-owned vessels operating under foreign "flags of convenience" may not be subject to requisition in time of emergency. In 1973, for example, the President of Liberia issued an Executive Order forbidding all Liberian-flag registered vessels from making deliveries to the Middle East. Even if these foreign-flag vessels could be requisitioned, their foreign crews, who often work for a pittance, may be unwilling to expose themselves to risk in order to advance U.S. interests. In a time of emergency, the United States cannot rely on a foreign-crewed fleet. In any case, these U.S.-owned vessels operating under foreign "flags of convenience" consist for the most part of vessels of very little military utility.

All ODS vessels with their 100% U.S. crews, on the other hand, must be enrolled in a sealift readiness program. And as U.S.-flag vessels, they can be requisitioned in a national emergency. By assisting the operation of these merchant vessels, the government avoids the enormous costs of acquiring and maintaining these vessels solely at government expense. Proposals to increase the Ready Reserve Force to the current target of 90 to 124 vessels call for annual maintenance costs nearly $1 million per vessel plus hundreds of millions of dollars for acquisition. A recent NACOA study supports the conclusion that the merchant fleet serves as the best source of sealift and recommends that the size and military usefulness of this fleet be increased. The report reasons that while surplus commercial vessels might be available for the RRF at low prices during the current shipping recession, annual maintenance would soon raise their real cost dramatically. An active fleet, on the other hand, is cost effective because the operator in trade bears the maintenance costs.

Modernization of the commercial fleet will improve the quality of vessels available for the NDRF and RRF. The 60 to 70 private liner vessels in good operating condition, but commercially obsolete for world trade, could be used to replace the large number of World War II era vessels (78%) which should be dropped from the NDRF.

Clearly, the U.S.-flag merchant marine is absolutely vital to all aspects of U.S. sealift capacity.

Senator STEVENS. Thank you. Gentlemen, does anyone else have any comments to make?

Mr. SKOURAS. Mr. Chairman, members of the subcommittee, my name is Spyros Skouras. I am president and chief executive officer of Prudential Lines, one of the seven U.S.-flag liner companies still in existence.

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Prudential Lines appreciates the opportunity to testify before you today at this build and charter program hearing on S. 1832 and S. 1833, two significant legislative proposals that could substantially help the current state of the U.S. merchant marine. We are encouraged by the subcommittee's continued support of and interest in the U.S.-flag liner industry.

Since 1972, the U.S.-flag liner companies in foreign commerce have been reduced in number from 20 to seven. The three small lines, Prudential, Farrell and Waterman Steamship, presently operate 16 vessels and are responsible for well over 6,500 jobs aboard ship and on shore. The three small lines presently account for approximately $400 million in annual revenues.

These factors are important and must be considered in any legislative program in order to prevent an unnecessary and disruptive impact on these small liner companies and on the jobs and labor which depend upon them.

Prudential believes that a build and charter program or a merchant ship revolving fund can be an important and effective program permitting the U.S. merchant marine to become more competitive in the world market. Prudential supports the thrust of S. 1832 and, with certain modifications discussed below, could wholeheartedly embrace the legislation.

However, Prudential Lines cannot endorse the build and charter program as outlined in S. 1833 because it does not provide a program that is responsive to the needs of the small liner companies for vessels or special assistance and is not a program that helps to ensure the viability of the small liner companies which are part of the U.S. merchant marine.

Therefore, my remarks are directed to S. 1832. S. 1832 provides for a merchant ship revolving fund to be established initially through the transfer of approximately $850 million from unobligated balances of prior year shipbuilding appropriations. This new revolving fund would be established to finance the construction of militarily useful commercial ships to supplement the National Defense Reserve Fleet. The fund would be allocated to the construction of vessels for the subsidized liners proportionate to certain liners' revenues in the year that the legislation is enacted.

The legislation would also establish a merchant ship working capital account for working capital loans upon terms and conditions established by the Secretary of the Navy for the three small liner companies.

We believe the working capital loan provisions should provide the needed financial assistance and be modified to include:

(a) a provision for a $15 million loan for small liner company;

(b) a provision for a greater loan if revenues fall below 5 percent of the 3-year average revenues for calendar years 1982, 1983, and 1984 at a ratio of 50 percent for each dollar lost;

(c) a finding that the need exists for the working capital loan;

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(d) a provision that the funds should be replenished and the loan discharged solely by payment for charter hire made by any participant; and

(e) a provision that no interest on this capital account shall be assessed or paid.

With these changes, Prudential believes that the build and charter program is a good one for the U.S. merchant marine and specifically for the small liner companies as it provides much needed guaranteed financing and provides for needed modern U.S. ships at competitive rates. In order to ensure the viability of small liner companies, Prudential believes that the ODS concept and the trade route concept should remain intact until all liner companies are fully competitive.

I must emphasize that the build and charter program legislation should specify that the small liner companies would be the first to receive new vessels.

While Prudential supports the grant of some limited flexibility to the Secretary of the Navy to determine the appropriate vessel designs for the build and charter program, Prudential does not believe that the Secretary of the Navy should have unrestricted authority to lease or charter the ships built through the fund to the U.S. commercial operator of his choice, nor should the Secretary be able to designate types of vessels for construction if those vessels would not be useful for oceangoing foreign commerce.

Therefore, Prudential could not endorse a build and charter program that did not specify that the small liners would be provided with new vessels on a priority basis over the large liner companies and one in which vessel selection was solely at the discretion of the Secretary.

With the changes discussed above, Prudential would support S. 1832 as legislation to provide much needed assistance to the U.S. merchant marine.

We are members of CASO and we support the general position that Mr. Lowman read. But we would not support it without these amendments that we are suggesting.

Senator STEVENS. Any other statements, gentlemen?

[No response.]

Senator STEVENS. Mr. Lowman, how many members do you have now, sir, in your group for subsidized liners?

Mr. LOWMAN. Well, we have five represented here.

Senator STEVENS. I mean how many companies are still involved in the operations of the subsidized lines?

Mr. LOWMAN. All of us, and Waterman as well—which would be six.

Senator STEVENS. Six.

Mr. LOWMAN. And then Sea-Land is unsubsidized.

Senator STEVENS. And how many would be considered smaller liner companies that you mentioned, Mr. Skouras? How many of those are smaller companies?

Mr. LOWMAN. Mr. Skouras has described that there are four larger companies and three smaller companies, although we take issue with that. We say we are an intermediate size company.

Senator STEVENS. What I am trying to get at—do we have seven altogether?

Mr. LOWMAN. That is correct.

Senator STEVENS. And what you are saying, Mr. Skouras, is that the three smallest ones must get their vessels first; is that right?

Mr. SKOURAS. Yes, sir.

Senator STEVENS. Why is that?

Mr. SKOURAS. Well, this program, the build and charter, if it is going to be of benefit to the liner companies, the liner companies that are in need of the most support right now as we see it are the three smaller lines. And the concept of deregulation in the ocean trade route concept, which is part of the CASO program that Mr. Lowman read, would give the right to the big lines through unlimited competition with subsidy on our routes.

The only thing that the small lines have is their protection from indiscriminate competition from American-flag operators. So we believe that the small lines should be put into a postion first where they can compete against the big lines, especially since their birthright, their contracts with the U.S. Government, their 20-year contract with the U.S. Government is going to be taken away from them, as is proposed by some members in the administration and some of the subcommittee.

Senator STEVENS. How many vessels are currently operated by all seven?

Mr. SKOURAS. I think it is about 125. Is that correct, George?

Mr. LOWMAN. I don't know exactly. It is over 100.

Senator STEVENS. And how many do the three smaller liner companies operate?

Mr. SKOURAS. We have about 16, under my definition of the smaller lines. I say anybody that does less than $200 million is a small line. When you consider that U.S. Lines and Sea-Land, do $1.5 billion, or APL does $1.5 billion, a $200 million line is not a very signficant line in my estimation

Senator STEVENS. Is there an agreement on the type of ship that ought to be built— whether for the large, medium, or small liner companies if this program is put into effect?

Mr. SKOURAS. I did not hear the question.

Senator STEVENS. I said is there an agreement on the type of vessel that would be built, without regard to whether they are for the small or medium or large size liner companies? Do you all think there could be an agreement on the type of liner to be built?

Mr. SKOURAS. I would think so. I think Prudential is ready to declare that they would be able to join in a program that would serve the military needs as well as the commercial needs as long as the price for that ship would be competitive to our foreign competition, even if it had features which the military insists upon that would make it a much more expensive ship.

For example, to carry the same amount of cargo in a ro/ro ship is much more expensive than in a container ship. And then you have additional operating costs for the extra fuel. These things have just been

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cranked into charter terms that would offset the military needs for the commercial needs.

Senator STEVENS. Mr. Lowman, what do the large carriers think about this position that the smaller liner companies should get the vessels first if this bill becomes effective?

Mr. LOWMAN. Well, in my statement, Mr. Chairman, I referred to build and charter legislation with some encompassing arrangements. And the ecompassing arrangements would provide for the larger companies, with those accompanying programs which would bring about deregulation, which would eliminate trade routes and give the larger companies additional benefits, including a wage adjustment, wage differential payment. Then they, in most part, would agree with the concept that the smaller companies would get the ships first, since they really at the moment indicated in prior meetings that they don't have an immediate building need.

Everybody has got a building need, but some needs are less immediate than others. The answer is that they would agree if they had the accompanying arrangements with it.

Senator STEVENS. Do you think the build and charter program must be integrated with a build foreign option window?

Mr. LOWMAN. I think so; yes.

Senator STEVENS. That would be primarily be used by the larger liner companies; correct?

Mr. LOWMAN. Well, it would be used by anybody that would not be accommodated by the build and charter program. I think, as we have indicated previously, we would commit to the build and charter program if we can have competitive equipment.

Beyond that, we would go to the foreign purchases, and the larger companies probably would go to foreign purchases immediately because they would not have the availability of the build and charter program as we have been discussing it initially. Possibly in later stages it would become available to them.

Senator STEVENS. Gentlemen, do any of the rest of you have any comments you wish to make this morning?

Mr. BLOCKLIN. I think Mr. Lowman, Mr. Chairman, hits this thing quite squarely. The amount of money that is available in the build and charter program, it seems to us, is probably finite. A first-year certain amount of money, and then perhaps this will be replenished by the chartering or the sales that are done, but I don't know how fast or how quick the replenishment will occur.

And given the need for the smaller lines to get some ships, I believe that—and you have heard Secretary Pyatt's testimony—there is probably a question of whether all of the funds that might be available in the initial creation of this build and charter fund would be available for the type and quantity of commercial ship that we all would want. Secretary Pyatt talked to us of small tankers, 36,000-ton product tankers, which we realize is a need for the Defense Department this too will absorb a portion of the build and charter fund.

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Mr. TAVROW. Mr. Chairman, I think that one point to emphasize as well, in full support of what Mr. Lowman said, is that, certainly for the larger companies, a key element to an all-encompassing program would be the ability to build ships for it. What clearly would happen, if that were part of a program that was enacted, would be the difficulty at least for the smaller companies to finance that kind of construction program.

The larger companies presumably would have more resources to call upon. Clearly, in that context, there would be no objection, at least by my company, to the smaller companies taking first advantage of the build and charter program.

Senator STEVENS. Senator Inouye.

Senator INOUYE. Thank you, Mr. Chairman.

How do you respond to the strong contention voiced by the unsubsidized liners, that a playing field would not be level if subsidized liners were permitted to take advantage of the substantially lower costs of building foreign or build and charter and retaining ODS eligibility?

Mr. LOWMAN. Well, I would agree that the playing field would not be level if the subsidized carriers have an ODS program and Sea-Land, the one unsubsidized carrier, does not have a subsidy of any kind.

And that is why in my basic remarks, I am talking about encompassing legislation which would involve a wage differential program which would be the same for each of us. Therefore, they would benefit to the extent of having a wage differential, which would make the playing field in their case level.

Senator INOUYE. What if they say they don't want subsidies?

Mr. LOWMAN. Well, I don't think anybody should be forced to take a subsidy. And if they don't want a level playing field and they want to work without one, fine. But I don't think because they take that position, they should preclude others from having the opportunity.

Senator INOUYE. One of the major problems faced by all of us is the over-tonnaging in both oceans. Would this program exacerabate that problem?

Mr. LOWMAN. I don't believe so, because the equipment that we presently have is desirable and needed and valuable to the Navy and would be part of the Ready Reserve Fleet. Even though the equipment is desirable and attractive to the Navy, it is not competitive for us and therefore it is technologically obsolete. We want to replace it

We would replace it with new competitive equipment. It would give us a better chance to compete. It would allow us to expand the merchant marine, and in the meantime the Navy would have equipment that would be available in the times of emergency with crews from our ships or supplemented from our ships would permit the manning of that equipment.

So there would not be an over-tonnaging insofar as the United States is concerned. There still would be over-tonnaging insofar as the world merchant marine situation is concerned, but we would be able to compete with it.

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Mr. TAVROW. Senator, I think it is clear that if these programs were enacted, in large part, as Mr. Lowman said, existing capacity would be replaced. Therefore, on net balance, at least in the near term, there probably would not be any additions to the overcapacity situation.

Senator INOUYE. Thus improving the quality.

Mr. LOWMAN. [Nods in the affirmative.]

Senator INOUYE. Are all of you in agreement that the unsubsidized operators should be provided subsidy in your program?

Mr. LOWMAN. We are all agreed that there should be some kind of a wage differential payment for everybody because everybody faces the same problem.

Now, whether everybody, in the final analysis will take it—because there are always a certain number of restrictions that are attached to getting anything—that remains to be seen. But basically we are generally in agreement that it is fair if American crews are desired—and we think they are—that the difference from a competitive of point of view with foreign crews should be made up by the Government.

And that should be in the form of a wage differential, and it would be at a lesser amount than the ODS that we presently receive.

Senator INOUYE. By "generally in agreement," you are suggesting that some are not in agreement.

Mr. LOWMAN. Well, Sea-Land has indicated a lack of agreement at this point. But they can speak for themselves because I understand they will testify here.

The rest of us have ODS. The rest of us need it. And we do not feel that we could function with American crews without some kind of a subsidy. We are now calling it a wage differential, which is slighty different from ODS.

Senator INOUYE. Thank you very much, Mr. Chairman. I have a few other questions I would like to submit.

Mr. LOWMAN. We would be happy to respond to them.

Senator STEVENS. We appreciate your testimony, gentlemen. We will keep struggling to see if we can find a compromise solution here.

Our next panel is Peter J. Finnerty, vice president, public affairs, Sea-Land Corporation; Tom Crowley, chairman and president of Crowley Maritime; and Harold Grehan, Jr., executive vice president of Central Gulf Lines, Inc.

And we also have Edward L. Merrigan, counsel, Central Gulf Lines, accompanying Mr. Grehan.

Gentlemen, who will speak first? Mr. Finnerty?

STATEMENTS OF PETER J. FINNERTY, VICE PRESIDENT, PUBLIC AFFAIRS, SEA-LAND CORPORATION, ACCOMPANIED BY WILLIAM F. RAGAN, COUNSEL, RAGAN & MASON; THOMAS B. CROWLEY, CHAIRMAN AND PRESIDENT, CROWLEY MARITIME CORPORATION; AND HAROLD S. GREHAN, JR., EXECUTIVE VICE PRESIDENT, CENTRAL GULF LINES, INC., ACCOMPANIED BY EDWARD L. MERRIGAN, COUNSEL

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Mr. FINNERTY. I would be happy to, Mr. Chairman.

Good morning. We appreciate the opportunity to appear today and in response to your request we will make an effort to summarize our remarks. We would like to present Sea-Land's views on S. 1832, the Council of American-Flag Ship Operators' build and charter proposal, and S. 1833, the build and charter proposal of the Shipbuilders Council of America.

Mr. Chairman, Sea-Land generally supports the concept of build and charter and our comments and suggestions are intended to be helpful to the subcommittee in its efforts to enact such a program. We believe an appropriately drafted build and charter program would clearly benefit all segments of the United States merchant marine industry.

It should provide much needed vessel construction work for U.S. shipyards, guarantee the availability of militarily useful commercial vessels to supplement the National Defense Reserve Fleet and its Ready Reserve Force, provide employment to U. S. merchant seamen, and provide operators in the U.S. foreign commerce with a source of competitively priced, commercially competitive U.S.-built vessels on a fair and even-handed basis.

Having said this, Mr. Chairman, no build and charter program will achieve these goals unless it is available to all segments of the industry and treats all similarly situated program applicants in an equal manner.

For this and other reasons, Sea-Land opposes S. 1832, the CASO proposal, and supports the approach of S. 1833, the SCA build and charter program, provided the concepts in that bill are properly expanded upon and spelled out in terms of their specifics.

Mr. Chairman, before discussing S. 1833 and the changes necessary, we would first like to point out what we perceive to be some of the most significant problems with S. 1832. Most importantly, S. 1832 would not benefit U.S.-flag operators as a whole. Specifically, it could not by its terms benefit any company in the bulk segment of our industry or the tanker segment, for that matter, and it could not be availed of by the majority of the liner segment.

Under section 2(g) of the CASO bill, the entire $850 million appropriated to the Merchant Ship Revolving Fund would be for the exclusive benefit of just four unaffiliated subsidized liner companies as defined therein.

The bill would further benefit those four companies by allowing them, but no other company, to trade in vessels to the National Defense Reserve Fleet or its Ready Reserve Force and receive a credit against the cost of chartering or purchasing vessels under the program. There are also questions about the valuation and certain other aspects related to the loans which are spelled out in our submitted comments.

Unlike the CASO proposal, S. 1833 is not designed to benefit specific companies or a specific segment of the maritime industry. Mr. Chairman, we will not take the subcommittee's time and discuss each section of the bill. Instead, we would like to highlight certain important sections and point out some clarifications and amendments which Sea-Land believes would greatly strengthen this bill.

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In this regard, we are attaching to these comments a suggested redraft of the bill with some of the proposed revisions superimposed. We do not consider the attached redraft to be in final form, since we have had only a very brief period of time to analyze the bill.

First, Sea-Land strongly endorses section 2(g) which makes vessels constructed under this program completely ineligible for ODS and section 2(h) which prohibits the Secretary of the Navy from selling or chartering the vessels to any liner operator, even for unsubsidized lines operation, unless they are needed to replace existing lines vessels.

However, since these new vessels would not receive ODS, for each vessel acquired, a subsidized liner operator's ODS service should be amended by making proportionate reductions on a vessel productivity basis in the number of subsidized vessels and the number of subsidized sailings.

The amendment to the bill would be consistent with and further the purpose of the 1970 Amendments to the Merchant Marine Act of 1936 of reducing liner operators' reliance on subsidy and President Reagan's statement of October 15.

A few points also require clarification regarding the purchase and charter price of the vessels constructed under the program. Pursuant to section 2(f), the purchase price of the vessel cannot be less than the cost of constructing the vessel outside the United States. Since foreign construction costs vary greatly from country to country, the bill should specify the standard to be used in making the required cost comparison.

With respect to the charter price of vessels, while section 2(d) does require competitive bidding, it does not set a minimum charter price. The inclusion of such a provision which relates to the usual commercial criteria would ensure that the Government receives a fair return on its investment.

As a final point concerning the cost of the new vessels, S. 1833, unlike the CASO proposal, does not permit a credit for trade-ins to the Ready Reserve Fleet. Sea-Land agrees with this approach.

Section 2(h)(2) should be amended, and I noted Senator Stevens' remarks at the outset that the coastwise reference has been deleted. We would strongly agree with that approach and we think that none of the vessels under the program should be used in the Jones Act trade. There should be no exception to that Jones Act prohibition, except a Presidential declaration of national emergency.

Fourth, it is essential that any build and charter proposal account for the fact that funding will be available only for a limited number of vessels. While section 2(b) empowers the Secretary to use the Fund for the construction of militarily useful commercial vessels, it does not set forth any other criteria to be used in choosing between proposals to construct different types of vessels. Such a clear statement of priorities is necessary to ensure that the vessels constructed have long-term commercial utility.

At a minimum, these criteria would have to encompass the following factors: (1) the military utility of the vessel; (2) the commercial competitiveness; (3) the need for the vessel in the trade in which it will be

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deployed; and (4) the potential for creating overtonnaging in the proposed trade with respect to vessels of the type proposed.

Fifth, we suggest that the bill be amended to require that the purchasers or charterers of the vessels constructed under the program be responsible entities. That is, a purchaser or charterer should be financially responsible in terms of its net worth and amount of working capital. It should also have a proven track record of operating vessels of the type to be acquired. This will promote the sale and charter of the vessels to entities with the knowledge and capability to guarantee maximum utilization of the vessels and prevent speculation.

Finally, S. 1833 limits the sale and charter of the vessels to U.S. citizens and we understand this to require that they be U.S. citizens as defined in section 2 of the Shipping Act of 1916, as is required by section 905(c) of the 1936 Act.

It is Sea-Land's position that this citizenship requirement is essential to ensure that the program only benefits the U.S. maritime industry and not foreign interests seeking to acquire these vessels through U.S. shell corporations.

Mr. Chairman, we appreciate the opportunity to appear today and would be happy to respond to questions.

Senator STEVENS. Thank you very much.

Tom, do you have a statement?

Mr. CROWLEY. Yes.

I am Thomas B. Crowley, chairman and president of Crowley Maritime Corporation.

Crowley Maritime is a large tug-and-barge company that provides common carrier transportation service between the mainland United States and Alaska, Hawaii, and Puerto Rico and contract tug-and-barge service throughout the world.

We presently hold contracts with the United States Navy to carry cargo to Alaska's Distant Early Warning Radar system, to Guantanamo Bay, Cuba, to the Azores, and to transport bulk petroleum by tug barge in the Far East. We are the primary carrier of modules, materials and supplies by water to the north slope of Alaska under contract to oil companies developing the oil resources of that region.

We have invested over $700 million in equipment and facilities and now operate over 400 vessels ranging from harbor tugs and supply boats to triple deck ro/ro trailer barges and double-deck railcar/trailer barges which are equal in size to many of the typical liner vessels operating in the world trade.

Senator Stevens and Senator Inouye, you are to be commended for your recent efforts to provide a program which will meet the urgent need of the carriers in foreign trade and the shipyards.

There is one aspect of the proposed build and charter program, however, on which I would like to comment. I note that the language in both S. 1832 and S. 1833 expresses the intent that ships built with the Merchant Ship Revolving Fund are for use in the foreign commerce of the United States (S. 1833) or in international commerce (S. 1832).

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Further, the Secretary of the Navy shall not charter or sell any vessels constructed under the bills for operation in the coastwide or intercoastal trade, except if the Secretary finds that it is in the interest of national security to do so.

I wish to go on record endorsing these restrictions on the use of such vessels in domestic trade including, by definition, the non-contiguous domestic trades. These restrictions are vital to the financial strength of existing carriers. Should it appear to the financial community that vessels acquired at world prices could enter the domestic trades, the value of our floating assets used in the domestic trades and for which we paid U.S. prices, would be immediately be discounted to the world price level.

Because of the critical nature of this matter, I would urge that section 1401(h) of S. 1832 and section 1401(h)(2) of S. 1833 each be modified to read as follows:

The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section or operation in the coastwise or intercoastal trade. However, if national defense considerations would otherwise warrant, the Secretary in Defense, in requesting the Secretary of the Treasury to waive the provisions of 46 USC 833 pursuant to the authority contained in the act of December 27, 1950, C.1155 1 and 2, 64 Stat. 1120, the Secretary of Defense may instead permit a vessel constructed under this act to be operated in coastwise or intercoastal trade for as long and only as long as such defense considerations continue to exist.

The purpose of this suggested language is to establish the same standard for permitting a vessel built under this program to operate in the domestic trades as for permitting a foreign flag vessel to do so. With the modification just suggested, we wholeheartedly support this legislation.

Thank you for this opportunity to testify. I will be pleased to answer any questions.

Senator STEVENS. Thank you.

Mr. GREHAN. Mr. Chairman, members of the committee, my name is Harold Grehan, Jr. I am executive vice president of Central Gulf Lines in New Orleans. We are an unsubsidized U.S.-flag shipping company owning ships and lash barges totaling 450,000 tons of capacity.

We appreciate the invitation to appear and commend you, Mr. Chairman, and the other members of the committee. You recognize the U.S. merchant fleet is in serious decline and legislation is needed.

We support your build and charter program. There are two versions: S. 1832, which we flatly oppose, as it is designed to assist the subsidized lines only. We can support and do support S. 1833, with added amendments and changes we feel are needed.

Since the $850 million would build only a limited number of vessels and many more are needed but unable to be built in U.S. yards, we support and propose building abroad, which requires removal of the 3-year prohibition requiring foregin-built vessels to wait 3 years before qualifying for preference cargoes.

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This action will cost the Government nothing, and open up the other building source needed to add to and strengthen the U.S. fleet. The fleet needs new vessels, not secondhand ones, if it is to be a first-rate fleet. Therefore, foreign vessels should be new and designs based on the need of the owner and the operator.

There should be no trading restrictions on new vessels, whether U.S. or foreign-built. Europe and the Far East are our major trading markets and there will be opportunities for new U.S.-flag vessels in these and other areas.

These three changes provide a quid pro quo for the U.S. shipyards and a realistic basis for giving the fleet a new start.

Finally, we do not feel these new generation vessels should receive operating differential subsidies. But if the committee decides to provide wage subsidy or SWAP to U.S.-flag operators acquiring new vessels under this legislation, then such subsidy should be made on equal terms to all, not just a few.

We sincerely the believe the work of your committee could not be more important to the future of our merchant marine. For our part, we are prepared to build new ships without delay when existing legal barriers are removed and all operators are on an even plane.

This concludes my statement. We thank you and are open for questions.

[The statement follows:]

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STATEMENT OF HAROLD S. GREHAN, JR., EXECUTIVE VICE PRESIDENT, CENTRAL GULF LINES, INC.

Mr. Chairman: my name is Harold S. Grehan, Jr. I am Executive Vice President of Central Gulf Lines, Inc. of New Orleans, Louisiana, and I appear before the committee today in place of our President, Mr. Erik F. Johnsen. Mr. Johnsen wanted to be here personally to present Central Gulf's views on the vitally important legislative proposals the committee has under consideration, but in line with long-standing business commitments, he is overseas and simply cannot attend.

From the very outset, we want to commend you, Mr. Chairman, and the other members of this committee who recognize that the U.S. flag merchant fleet is in serious decline, and that all available legislative actions should be taken immediately to reverse the present disastrous trend. Clearly, if the U.S. merchant marine is to survive and again compete effectively, it must be allowed to acquire new, modern vessels at prices it can afford to pay.

Existing economic conditions, including extremely high construction costs, construction delays and the recent demise of the federal construction subsidy program, plainly make it impossible for U.S. flag operators to finance and build the ships they desperately need in U.S. shipyards. Simultaneously, the federal cargo preference laws effectively preclude the purchase and addition of new, attractively-priced foreign-built ships to the U.S. flag fleet. Under the existing cargo preference statutes, new foreign-built vessels are prohibited from transporting preference cargoes until they have been documented under the laws of the United States for three (3) years. Automatically, therefore, for three (3) years these foreign-built U.S. flag ships are unable to compete fairly and economically with other U.S. flag vessels—even those in serious need of replacement—which are eligible under the outdated statute to carry preference cargoes.

Consequently, while Central Gulf: (i) flatly opposes S. 1832 proposed by the Council of American Flag Ship Operators; and (ii) feels that substantial amendments are necessary to make S. 1833 proposed by the Shipbuilders Council of America acceptable, salutary legislation, it nevertheless submits that the basic Build and Charter concept envisioned by Chairman Stevens should be expeditiously considered, fashioned and enacted by the Congress as perhaps the only available cornerstone or foundation upon which to base a new, strong, highly competitive U.S. merchant fleet.

Essentially, therefore Central Gulf urges the committee to draft and report new legislation of its own which will:

(1) Establish a Build and Charter Program to consist initially of the $852,300,000 fund earmarked last month by the Defense Appropriation Committtee, such program to operate generally as provided in the Shipbuilders' bill, S. 1833. Under that program, a limited number of new U.S. flag merchant vessels will be constructed in U.S. shipyards for charter or sale to United States citizens at reasonable, competitive prices or rates roughly equivalent to prices charged for similar vessels constructed abroad.

(2) Remove the 3-year statutory prohibition which presently precludes the transportation of preference cargoes in new U.S. flag vessels constructed abroad. This is imperative because the Build and Charter Program will provide only a limited number of new ships; others must be constructed abroad to meet the minimum needs of the U.S. merchant marine. Removal of the 3-year barrier is necessary to assure these new vessels are built. To reap the broadest possible benefits for the United States, its repeal must apply to truly new, modern foreign-built ships, and not to old vessels that are merely rebuilt or reconditioned abroad. Moreover, U.S. flag operators must be free to build abroad the type of vessels they actually need in their operations, and there should be no unnecessary discriminatory restriction.

Finally, the antiquated, oppressive 3-year bar must be lifted now, as a quid pro quo for the extensive benefits the domestic shipbuilding industry will realize under the new Build and Charter Program.

(3) Provide that U.S. flag operators who charter or purchase Build and Charter Program vessels, or who acquire new foreign-built U.S. flag vessels under the legislation, shall not be eligible to receive rating Differential Subsidy payments for the operation of such vessels. As Chairman Stevens recognized when he introduced S. 1832 and 1833 on November 5, the entire new program must be fashioned to prevent the granting of unfair competitive advantages to one U.S. flag vessel over another.

If, on the other hand, the committee decides to provide for the payment of operating differential subsidy payments, or SWAP payments etc., to U.S. flag operators who acquire new vessels under the legislation, then patently the committee must

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provide "a level playing field" open to all competing U.S. flag operators. Such subsidy support must be made available on equal terms to all—not to just a chosen few.

In conclusion, Central Gulf submits that, in the national interest, the committee should go forward and complete its legislative work in this area at the earliest possible moment. The committee should urge the exising subsidized segment to come to terms with the unsubsidized segment to afford unanimity of the maritime industry. When all is said and done, every reasponsible industry representative will almost surely agree that action must be taken without further delay to revitalize the U.S. merchant marine and to provide for the replacement of this nation's obsolescent merchant fleet. We honestly believe that enactment of legislation such as that outlined in this statement will accomplish that goal for the benefit of all segments of the industry. Central Gulf's interest in this matter is not academic or parochial in any sense. We are prepared to build several new ships without further delay, but we can proceed only then the existing economic and legal barriers are removed.

Senator STEVENS. Senator Inouye, do you have questions?

Senator INOUYE. Although the measures before us do not cover the so-called SWAP program, obviously the SWAP program is lurking in the background.

Mr. Finnerty, may we have for the record your reasons for supposedly opposing the SWAP program?

Mr. FINNERTY. Senator, I would be happy to enumerate our reasons to whatever detail and extent you would like. I would like to say initially that our Chairman has stated on several occasions that it is his impression, having analyzed the programs and the situation in the merchant marine today, that the best answer for the industry would be movement away from the older programs to an approach that would minimize the intrusion of the Government into the merchant marine and lessen dependence upon subsidy.

Having said that, in trying to focus on the specifics of the proposal, we would say that it can be assumed that a funding for any kind of SWAP program or a similar program in the coming years would be limited and would likely not exceed current MarAd funding levels. Under SWAP, at least 111 vessels would receive these kinds of government payments, and if each vessel were to receive—I think some calculations or estimates have been in the neighborhood of $3 million as an estimate—the total annual cost would exceed $333 million.

The administration's MarAd budget request for fiscal year 1986 was $286 million or $46 million less than would be required intially. The proposal also ignores funding realities. You made a reference earlier, Senator Stevens, to OMB's reactions just to the build and charter program. The expansion of the program beyond the existing companies would be a constraint.

Secondly, contracts, as we understand the proposal, would terminate 15 years from the date of enactment, but could be renewed for additional periods of time. Thus, the program could potentially last for an extensive period of time, 30 years or more.

Vessels chartered to MSC and all ODS vessels in operation or laid up would qualify for SWAP under the program. By comparison, only nonsubsidized vessels actually in operation in common carrier service, would be eligible. That is another inequity.

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During the 3-year transition period that is proposed in the package, vessels under subsidy contracts would receive full ODS payments and their replacements would receive full SWAP payments. By comparison, the manner in which they would treat nonsubsidized companies and nonsubsidized vessels and their replacements would provide only percentages. I think the numbers are one-quarter, one-half, three-quarters, et cetera over the 4-year period of time.

During that proposed transition, all restrictions and obligations imposed upon the ODS operators by their contracts would be terminated, even though their contract vessels would continue to receive the full ODS level of payments. This would again penalize the unsubsidized operators who would not receive SWAP payments until after this extensive period of years for transition.

The proposal establishes caps on the number of vessels per operator which could receive these SWAP payments. These caps could be circumvented by acquiring or combining with an unrelated company.

The bill grandfathers in all existing 805 rights and authorizes the Secretary to enter into new title XI guarantees with respect to these SWAP vessels. Again, these are implications which are unfair from the point of view of a a non-subsidized carier.

Those are initial reactions. It is a very complicated proposal, as you know, but if you would wish, we could go into more detail.

Senator INOUYE. The Chairman and I on many occasions have indicated our desire that the industry come forth with some sort of consensus, some arrangement that all of us can agree upon.

Do you believe that such a consensus is not possible? Or is it possible to have a consensus?

Mr. FINNERTY. Senator, I would say that in the years that I have been involved in the industry, there have been numerous occasions where certain changes or attempts at reform have not seemed possible, and yet with time and with discussions, it eventually worked out.

My own opinion is that I would think that if continued discussion and analysis takes place, and if the industry can overcome its parochial attitudes, I would have to believe that something can be worked out.

Senator INOUYE. Are discussions ongoing at this moment?

Mr. FINNERTY. I don't think it is fair to say that discussions are ongoing that include the non-subsidized lines. I understand that there has been considerable discussion and negotiation by many of the people in the industry, but there are no formal discussions at this time that I know of.

Senator INOUYE. Is Sea-land prepared to enter into confidential discussions with other subsidized and unsubsidized lines?

Mr. FINNERTY. Again, Senator, I would repeat, the basic answer is yes. Our Chairman, I understand, indicated to yourself and Senator Stevens at your October discussions, his willingness to enter into discussions with other entitities in the industry, with the understanding that the discussions would be for the purpose of arriving at a fair, even-handed approach in trying to reach a solution.

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Senator INOUYE. I think the moment has come during the festive season of happiness and love.

Thank you very much.

Senator STEVENS. Senator Long.

Senator LONG. No questions.

Senator STEVENS. Gentlemen, many of the industry representatives have said to me that they think any legislation should be aimed toward preserving and protecting the competitive environment among our maritime interests.

Do any of you have comments about additional procedures that ought to be included in legislation of this type to protect the competitive environment, the so-called even playing field?

Mr. GREHAN. Mr. Chairman, I would like to make one comment and that has to do with the freedom, if you will, of the trade route concept. Currently, the existing susidized lines are now attempting, as I understand it, to open up the trade route concept which would in effect give them unrestricted trading opportunities.

This is one of the principal reasons that we declined the subsidy many years ago, because we elected to remain deregulated.

Now it seems that the subsidized lines are attempting to put themselves in a deregulated position and take the subsidy as well, so this is another element of a problem that I think should be resolved in a fair way.

Mr. FINNERTY. Senator, could I add a comment to that, please?

Senator STEVENS. Surely

Mr. FINNERTY. In thinking over a couple of the questions that were asked of a few of the earlier witnesses, I would want to indicate that in our opinion it would be disruptive and depart from a fair competitive marketplace if the build-foreign type proposal were coupled with the build and charter program for the subsidized carriers.

If that were done, it would leave the unsubsidized liner operators in a distinctly disadvantageous position.

Senator STEVENS. Senator Inouye asked you about SWAP. Would you support SWAP if it did not have a transition period?

Mr. FINNERTY. I think that the transition period is certainly a serious problem in the proposal, Senator, but there are other elements of the proposal that would require some clarification, that are ambiguous. Assuming that they were worked out in an even-handed and fair fashion, I would think that it would move very close to a solution to the differences in the industry.

Senator STEVENS. The ODS route regulations are a substantial burden, are they not, to the subsidized carriers?

Mr. FINNERTY. We are speaking of the essential trade routes, Senator?

Senator STEVENS. Yes. The overall regulatory concept of ODS.

Mr. FINNERTY. Well, my feeling is that it really is not a burden in the sense that, like us, they can depart from those restrictions any time they choose. But the option that is available to them is one that they do not choose to exercise. So if there are those restrictions, they are self-imposed.

Senator STEVENS. Do you want to say something, Bill?

Mr. RAGAN. Senator, I might add to that if I may. The reasons for the restrictions was to make allowance for those who are not taking subsidy, to give them some protection while the Government was paying these particular lines.

It may be somewhat of a restriction or a burden, but it is imposed not as a restriction or a burden, but to give the other operators a fair shot.

Senator STEVENS. This is Mr. Bill Ragan, an attorney.

If there is no transition period, unsubsidized carriers would still have an immediate protection, would they not?

Mr. RAGAN. You are talking then about a SWAP program?

Senator STEVENS. Yes.

Mr. RAGAN. Yes.

Senator STEVENS. Gentlemen, we will have some additional questions to submit to you. It does seem to me that there has to be some way to tie in SWAP and make it possible to eliminate some of the problems that are involved.

I don't know if my colleague is going that direction or not. We will have to find that out.

Senator INOUYE. I think the solution lies in this room, sir.

Senator STEVENS. Well, we are hopeful. Does anyone else have any questions or statements?

[No response.]

Senator STEVENS. We thank you very much, gentlemen, and appreciate your courtesy. All the statements will be printed in full in the record, of course.

The next panel is Frank Drozak, president, Seafarers International Union of North America; C. E. DeFries, president, National Marine Engineers' Beneficial Association; and James F. Paterson, vice president, National Maritime Union of America.

I am informed Mr. Paterson has not arrived yet? Is he here?

[No response.]

Senator STEVENS. Gentlemen, we will proceed. If Mr. Paterson arrives, he will make his statement. If not, we will ask him if he wants to put a statement in the record.

Good morning, Frank.

STATEMENTS OF FRANK DROZAK, PRESIDENT, SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA, AFL-CIO; C. E. DEFRIES, PRESIDENT, NATIONAL MARINE ENGINEERS' BENEFICIAL ASSOCIATION; AND JAMES F. PATERSON, VICE PRESIDENT, NATIONAL MARITIME UNION OF AMERICA

Mr. DROZAK. Good morning, Mr. Chairman. Fine-looking committee this morning.

Mr. Chairman, on behalf of the Seafarers International Union, I would like to express our appreciation for the opportunity to present our views on the build and charter proposals contained in S. 1832 and

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S. 1833. I would also like to commend this subcommittee for its continuing effort to advance the interests of the U.S. maritime industry and thereby, the interests of our nation.

The intent of these proposed legislative vehicles clearly recognizes the dual role of the U.S. merchant marine by requiring that the vessels possess maximum military utility while operating on a commercial basis. A tank is a necessity for combat but has no productive peacetime role. A properly equipped merchant vessel, however, can serve not only as an effective instrument of war, but also as an effective instrument of peace and commerce as well.

Merchant vessels, which comprised two-thirds of the ships used by the Royal Navy in the Falkland Islands war and were essential to the success of that campaign, were described by the British Admiralty as "force multipliers." We have stated many times our belief that they are employment multipliers as well and also contribute to maintaining peace by providing a ready military auxiliary.

Our principal adversary, the Soviet Union, has long recognized the national security significance of a viable merchant marine and national defense features are standard design elements for newly-built Soviet merchant vessels. The construction and operation of a fleet as outlined in these legislative proposals, will undoubtedly be viewed by the Soviets as a significant contribution to American seapower and, as a result, the dangerous imbalance between U.S. and Soviet merchant marine assets will have been partially redressed.

The final design of any build and charter program will undoubtedly result from the process of consensus building that is the essence of our democratic process. While the SIU fully supports the concepts embodied in S. 1832 and S. 1833, we believe it critical that several key elements be included if a build and charter program is to be successful.

First and foremost is the necessity that all sectors of the fleet be eligible to participat in, and benefit from a build and charter program. We must ensure that dry bulk vessels, which can guarantee essential imports and provide cost effective transport for U.S. food aid cargoes, and militarily useful product tankers are made a part of any program. Multipurpose ro/ro vessels as well should be included, since they can be used for carriage of imported automobiles commercially while prepared to carry the large amount of rolling stock needed for military operations.

In addition to the classes of vessels, consideration should be given the various avenues of commerce that should be open to vessels built under a build and charter program. For example, it might be feasible to allow these vessels to enter certain trades where no other American operators are currently engaged. One that immediately comes to mind is the intercoastal trade, such as the East Coast and the West Coast movement, where no U.S.-flag operation presently exists.

The establishment of a build and charter program providing vessels constructed in U.S. yards, using U.S.-made components, for the U.S. merchant marine, will provide much of the critical work needed to maintain a viable shipbuilding mobilization base. It will also create

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employment opportunities necessary to provide an adequate pool of trained sea-going professionals with experience using the national defense features necessary to suport a U.S. military operation.

Recently implemented programs such as the Fast Sealift Ships, Maritime Prepositioned Shipos and TAGOS, have proven the validity of utilizing merchant marine personnel in support of military operations. We think a build and charter program is a logical next step and would further enhance U.S. military readiness.

The economics of a build and charter program are highly favorable. Although the Federal Government would incur some initial outlays to implement the program, the revenues returned to the Treasury from the sale or charter of these ships, the corporate tax revenue of the operating companies and those companies building the ships, as well as the payroll taxes of shipyad workers and shipboard personnel would repay those costs and provide long-term benefit.

It must be remembered, however, that a build and charter program can only be effective if it receives the full support and backing of the U.S. Government. While a build and charter program can provide the vessel types needed for national security purposes, the commercial function of those vessels still confront the dilemma of inadequate cargo volume. Thus, it is of vital importance that a solution to this problem be sought as we seek remedies for inadequate sealift assets.

Such support must include an adequate pool of government-impelled cargoes, as well as a commitment to actively negotiate bilateral shipping agreements with our trading partners. In addition, the Government must provide any training deemed necessary for personnel operating national defense features such as underway replenishment and specialized cargo handling equipment. It is also critical from the standpoint of national security that these vessels be fully crewed and operational at all times.

While we know that this subcommittee has always strived for a balanced approach to maritime policy, we would urge that the final form of any build and charter program take into account the views and concerns of all interested parties. We are well aware that alternate proposals have included both a wage subsidy component and a limited authority for certain U.S. operators to build vessels abroad in foreign shipyards.

For many years we have worked diligently to provide a reasonable measure of support for the U.S. shipbuilding industry. The reality of world shipping economics, however, are so overwhelming that a thorough review of existing policies can no longer be avoided.

One need only look at the alarming and continuing decline in the share of foreign commerce carried by U.S. flag vessels to appreciate the urgent need for immediate action. To stand idly by and do nothing will serve only to guarantee the death of this industry. It is for these reasons, therefore, that we urge the subcommittee to move foward with consideration of the proposals that have been discussed during recent industry meetings initiated by this subcommittee's leadership. These proposals not only included a build and charter program as outlined by

the bills before us today, but also a build and charter program coupled to a limited build-foreign authority.

Before concluding, Mr. Chairman, I would like to take this opportunity to briefly comment on two other items of extreme interest that while not presently before this subcommittee today, have received considerable attention in recent years.

As this subcommittee knows, there are but two active passenger ship vessels in the U.S. fleet. This is a tragedy not only for America, but for its national security as well. I believe that we now have a window of opportunity to at least partially remedy this situation. However, that opportunity will not remain open forever.

Presently, there are nearly 50 foreign-flag ships operating out of American ports. Unless something is done to provide a competitive U.S.-flag operation, I believe that American companies will be unable to break the virtual stranglehold foreign-flag lines have on this market. I would therefore urge that this subcommittee address this crucial issue in the very near future.

Secondly, Mr. Chairman, we take note that the Defense Subcommittee has set aside a pool of money to be used for the acquisition of liner vessels for addition to the Ready Reserve Fleet. We believe a more sound approach would be identify vessels in the existing fleet as candidates for re-engining and continued operation. This approach is suggested as a means of addressing the Department of Navy's stated concern over the lack of active vessels with fully qualified crews available at a moment's notice. Again, we would urge the subcommittee to at least give consideration to this option.

In conclusion, Mr. Chairman, we would like to strongly reaffirm our commitment to work with ship operators, shipbuilders, military experts, and the members of this subcommittee to develop a fair, effective and comprehensive maritime program. I believe that today's hearing as well as the recent industry-wide meetings, are a good first step toward our ultimate goal—a strong and healthy U.S. merchant marine.

Also, Mr. Chairman, as your letter indicated, I will be submitting additional information within the next 10 days. Thank you very much.

[The following information was subsequently received for the record:]

POSITION OF THE SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA, AFL-CIO

Over the past five years, major changes have been made to long-established national maritime policies. The industry has witnessed the demise of traditional promotional programs which have been the cornerstone of the nation's maritime policy without replacement by viable alternatives. Maritime policy is being approached on a piecemeal basis with no consideration given to the impact of prospective changes to all segments of the industry—liner, tanker, bulk, domestic, offshore, fishing, shipbuilding, and labor. Unless positive steps are taken to develop a maritime policy beneficial to all sectors of the industry, the U.S.-flag fleet will continue to wallow in the depths of a world shipping depression.

What is needed is a cohesive and comprehensive national maritime policy that is tailored to the realities of today's international shipping world and to the economic, political and military needs of the United States. Such a policy should address and benefit all facets of the maritime industry—from shipping to shipbuilding and related trades—in an integrated manner, so that there are no portions of that policy which will work at cross purposes.

This policy, which will serve as a solid foundation for the complete redevelopment of the industry, should consist of the following key elements:

Cargo.—The essential ingredient of a new comprehensive maritime program is the development, implementation, and enforcement of a national cargo policy premised on the internationally accepted and practiced principle of allocating a portion of a nation's foreign waterborne cargo exclusively to national-flag vessels. Guaranteeing cargo for U.S.-flag vessels will provide the wherewithal to preserve and enhance the nation's oceanborne transportation network and supporting shipyard capability by stimulating a climate for private investment in the construction and operation of new, technologically sophisticated and competitive American-flag vessels.

For example, the apportionment of cargo to vessels constructed under a build and charter program as well as to vessels in the Ready Reserve Fleet would guarantee active, available vessels and a pool of skilled, available seamen to meet any national emergency.

Assuredly, the guarantee of cargo is basic to the continued survival and future growth of the U.S.-flag merchant marine and commercial shipbuilding base, essential and integral components of the nation's defense and economic security.

Bilateral Agreements.—As part of an overall strategy to assure cargo for U.S.-flag vessels, the government should negotiate on a case-by-case basis bilateral shipping agreements with its trading partners with the goal of increasing U.S. shipping capability. These agreements are flexible two-way commitments to certain rules for trade. The goal is to obtain a reasonable share of the market with equal access to cargo and reciprocal treatment of national carriers within a set of terms acceptable to both nations and applicable to a particular situation. Bilateral agreements will guarantee a share of cargo to national-flag carriers, ensuring U.S. access to a trading partner's waterborne commerce.

Auto Carriers.—Initiate bilateral trade negotiations with Japan to open up the vehicle carrier trade between the United States and Japan to include participation by U.S.-flag operators in long-term, core vehicle transportation contracts. An agreement that would provide for equal carriage of imported Japanese cars on U.S. and Japanese vessels would afford American vessel operators an opportunity to gain access into the heretofore restricted car-carrying market of the approximately 1.85 million Japanese cars imported into the United States yearly.

Subsidy.—Several years ago, several operators asked for and received partial relief from the domestic building requirements for their replacement vessels. Congress granted this relief on the premise that it would permit U.S. liner companies to compete more effectively and efficiently with highly subsidized foreign fleets. While this temporary build foreign authority has placed American-flag companies on a more equal footing with their foreign counterparts, it has not entirely solved the problem of unfair competition. Recognizing that fierce competition remains unchecked, it is apparent that a thorough and timely review of the Operating-Differential Subsidy program be undertaken with the purpose of placing all U.S.-flag liner companies on an equal footing to better enable them to remain solvent in a highly competitive international shipping arena.

Build and Charter Program.—Establish a clear requirement for shipbuilding capacity for U.S. national security. This should be done as soon as possible in order to prevent the loss of facilities and skilled workers needed to maintain that capacity.

This could be accomplished by initiating a Build and Charter Program wherein the Secretary of the Navy would be authorized to finance the construction of militarily useful commercial vessels to supplement the national defense reserve fleet for

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charter or lease to commercial vessel operators. This program would have a dual purpose. First, it would provide employment for U.S. shipyards, U.S.-flag vessels for the carriage of the nation's waterborne commerce, and needed billets for unemployed merchant seamen. Second, it would strengthen the nation's defense security since it would have at its disposal in time of war or national emergency militarily adaptable commercial vessels manned by available experienced crews to meet contingency sealift plans.

Naval Supply and Support Vessels.—Continue to promote and implement the transfer of naval supply and support ships to private commercial vessel operation. The performance of private sector vessels and crews in current sealift roles proves the wisdom of expanding commercial support for naval operations.

The U.S. merchant marine is dependent on government contracts during this current prolonged and acute shipping depression. In turn, the Department of Defense depends on the U.S. merchant marine as the primary resource for military sealift needs. Therefore, transferring to a cost-effective private sector those programs and tasks unnecessarily performed by a contracting government workforce assists in restoring the U.S.-flag fleet and serves a mutual need.

Service Contract Act.—Support the consistent application of the wage provisions of the Service Contract Act to all government contracted marine service contracts. Judicious application of the Service Contract Act will ensure that any economic gains realized by the government will be the result of cost-effective management techniques rather than the result of substandard wages paid to merchant seamen.

Passenger Vessels.—Develop a policy of incentives to stimulate and expand the U.S.-flag passenger liner trade. This could be accomplished by permitting for a set period of time the return of formerly U.S.-built passenger vessels with domestic trading privileges as well as the reflagging of a select number of foreign built vessels. Such provisions should incorporate the requirement that the conversion work necessary to insure that reflagged vessels conform to U.S. safety and inspections standards be performed in U.S. shipyards. Likewise, routine maintenance and repair work on these vessels should also be performed in domestic shipyards. Finally, all reflagged vessels should be both commercially viable and militarily useful.

Capital Construction Fund.—Preserve the Capital Construction Fund program established pursuant to Section 607 of the Merchant Marine Act of 1936 and allow tax-deferred deposits in the fund to be used to construct in U.S. shipyards vessels for the foreign and domestic trades, excluding the inland waters of the United States. Presently, these monies are limited to the foreign and domestic offshore trades.

Exclusive Economic Zone.—Consistent with the President's proclamation extending to 200 miles the U.S. exclusive economic rights over exploration, exploitation and management of the natural resources of the seabed and subsoil, the Jones Act should also be extended to cover this 200-mile exclusive economic zone. Currently, Jones Act jurisdiction extends only three miles off shore, while most other major maritime nations claim anywhere between 12 and 200 miles as their navigation territory.

Jones Act Reaffirmation.—Support of the Jones Act as the backbone of Federal support for the United States domestic fleet which provides critical work to the commercial yards. This law has provided a strong defense-ready fleet for national security purposes, while guaranteeing reasonable domestic shipping rates through competition between domestic shipping lines.

Maritime Security.—Enact legislation requiring specific security measures to protect ports, vessels, passengers and crew members from terrorist attack. The government, in conjunction with maritime labor educational facilities, should initiate a training program to prepare merchant seamen to be alert to the dangers of terrorist activity, methods in which to prevent terrorist seizure and control of a U.S.-flag vessel, and the manner in which to handle the situation should a vessel be seized. In conjunction with this unilateral action, the government should negotiate international agreements seeking worldwide cooperation in bringing terrorists to justice.

Fishing Fleet.—The U.S. domestic fishing and canning industries must be encouraged to expand and programs to protect these industries from unfair foreign competition must be put into place. Despite existing legislation which extends the U.S. fishing zone and restricts foreign fishing fleets from operating in U.S. waters, heavily subsidized foreign industries continue to make inroads into the U.S. market.

It is evident that there are divergent viewpoints within the industry on what is the best policy to promote ship operations and ship construction. Careful consideration of these recommendations would provide new opportunities for work in U.S. shipyards. Under these proposals, U.S.-flag operators would be able to compete more effectively with foreign operators.

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In keeping with our previous position that changes should not be made to existing programs without viable alternative policies, we feel that these recommendations if adopted would permit us to support changes to long-established maritime policies.

Senator STEVENS. Thank you very much.

Gene, good morning.

Mr. DEFRIES. Good morning. Thank you, Mr. Chairman and members of the Senate, for this opportunity to be here today.

Mr. Chairman, I am pleased to testify today as President of the National Marine Engineers' Beneficial Association which represents more than 10,000 merchant marine officers. Before I begin with the subject at hand, S. 1832 and S. 1833, I would like to personally thank you and Senator Inouye and every Senator on this committee who provided their support during the recent Senate debate over the cargo preference compromise.

Not only was this support effective, but it has helped to achieve what I believe will be a highly productive solution to a long outstanding and often bitter dispute. This compromise demonstrated something else equally important in the context in which we meet today. It demonstrated that our industry—labor and management, bulk operators and liner operators, shipbuilders and ship operators—can work together to achieve a solution that benefits the industry as a whole. It is this kind of cooperative spirit that I hope we can bring to the discussion today of the bills that you have introduced.

Having said this, Mr. Chairman, I would like to raise a number of problems, general as well as specific, that I have with these bills as currently conceived.

Let me say, Mr. Chairman, that I support wholeheartedly the concept of build and charter. It was enormously successful with the Mariner program in the 1950s, and it can be successful today. It is the right way to go if we are serious as a nation about having a merchant fleet as a viable defense asset.

You have heard it said before, but I will repeat it today: It does no good to have a fleet of merchant vessels tied up in reserve in Beaumont Bay or on the James River if we do not have the crews to sail them. Modern cargo vessels are highly technical and extremely complex. You cannot just run out on the street and police up untrained men and women to run a modern ship, anymore than you can do that with pilots and mechanics to fly and service a C5A.

With our enormous commercial air industry, however, we have the kind of personnel and expertise base so that you could stockpile cargo planes and break them out on relatively short notice. We do not have anywhere near that kind of personnel base in our commercial maritime industry, and what base we do have is dwindling fast. As the fleet shrinks, crew sizes are getting smaller and will continue to get smaller as trained mariners retire.

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So build and charter provides a way to address this problem by creating operating vessels, not a mothball fleet. However, it is not enough to create such operating vessels. These vessels must be commercially viable or as much as we can make them, lest the program you propose become an intolerable drain on the Treasury.

This leads to what I believe is the single most important weakness of these pieces of legislation—they are silent on the subject of cargo, silent on how we will put cargo on the ships that are built. Without a new source of cargo for these vessels, we will simply have more ships trying to carry the same amount of cargo, and that would be a disaster for our fleet and an outcome you could not possibly intend.

The world is already suffering from a massive shipping depression brought on by overtonnaging in the world market. This overtonnage situation basically has far too many vessels chasing far too many cargoes. The situation is so bad that more than 60 million dead-weight tons of merchant ships are laid up around the world, some three times the tonnage of our entire fleet.

In the face of this situation, the U.S.-flag fleet has been fortunate that the Jones Act and vital cargo preference laws have served to help our fleet during a time of cutthroat competition brought on by world oversupply. But a new element of American vessels competing for the same reserved cargo could put much of the fleet at risk unless the introduction of these vessels is accompanied by measures to generate increased cargo.

Now, there are several ways to generate this cargo: increased government cargo allocation, adoption of the UNCTAD Code of Conduct for Liner Conferences, or bilateral shipping agreements. I personally favor bilaterals, included as a part of a national trade policy to promote American exports and services.

By contrast, the administration for five years has steadfastly opposed all of these cargo allocation measures. It has even gone so far as actually to attempt to undermine existing preference laws concerning agriculture and defense cargoes.

I believe that any legislation to create a build and charter program must have as an essential component, a cargo enhancement policy to go with it. The inclusion of such a policy would not only help widen support within our industry, but it would do much to create the national maritime policy that has been so clearly absent during the last 5 years.

Indeed, the fact that we are all here today discussing these proposals testifies to the absence of any coherent policy—a policy that ought to have come from the other end of Pennsylvania Avenue a long, long time ago.

In addition to a cargo policy, any build and charter program must see that the vessels themselves are vessels economically viable in the world trades. In this respect, having only the Navy determine the vessels to be built through such a program will probably lead to goldplated ships, unsuited for any trade in which the U.S. flag is viable.

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I would recommend that the Secretary of Transportation or the Maritime Administrator be included in vessel selection, as well as a strong measure of industry input. Vessels selected should be designed so that they can be converted to military use in short order if need be, through devices such as flat racks, sea sheds, or Arapaho. But we should not attempt to field a fleet of perfect militarily useful vessels. As we all know, we can convert vessels from merchant use to military; it is awfully hard to make a container ship out of an aircraft carrier.

Use of vessels such as roll-on/roll-off vessels that cannot come close to making a commerical go of it under the American flag would result in a fleet that cannot be sustained over time, and if we field these ships under this program we will only prove once more that the best is the enemy of the good.

These have been some general thoughts on improvements to these build and charter proposals. There are also a number of smaller, but still important, technical problems that must be resolved or clarified before these bills could win widespread industry support.

For example, clear-cut definitions in any legislation promoting our maritime industry are vital. Yet, in both these bills, citizens are able to negotiate charters from our government for vessels constructed under this program. Citizens may even buy these vessels. But what qualifies one for citizenship? The bills simply do not explain. Can a foreign shipping company set up a U.S. subsidiary here, hire an American president, and qualify for citizenship and gain profit through the use of American taxpayer dollars? This is certainly not the bills' intention. But unless words like "citizen' and "international commerce" are clearly defined, intentions will certainly fall prey to abuse.

Ambiguities in these bills also raise serious concerns. In both bills, the cost of chartering a vessel under this program is said to be less than what the Secretary of the Navy determines to be the cost "had the vessel been constructed outside the United States." There are numerous countries throughout the world with shipbuilding capabilities and at very variable costs. On what do we base the chartering or purchasing price of build and charter vessels? This point obviously needs attention.

Furthermore, these bills appear to have unnecessary and questionable restrictions in them. Why, for instance, does the program's revolving fund allocate money for the construction of vessels for charter or sale to persons who were parties to operating differential subsidy contracts for the operation of liner vessels only? I am certain that military experts would agree that the use of bulk vessels to carry strategic minerals, fuels, or to provide other military support during a crisis warrants that they, too, be included in this subsidy program.

S. 1833 does not, with very limited exceptions, allow build and charter vessels to receive operating differential subsidies at all. When the industry had construction differential subsidies, ODS was a natural complement to it. Why is ODS excluded under this legislation? And is it in the interest of the industry that it be excluded?

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S. 1833 also forbids the operation of these build and charter vessels in two of America's most important trades, except under certain limited circumstances. Again, I must ask: why? Doesn't such a restriction drive these vessels further away from a necessary goal of this program, which is "commercial viability?"

I would also note that if this program is intended to help our ailing shipbuilding industry, it seems desirable that some provision be made to assure that the most depressed shipyards get a fair share of the program's benefits. This may mean making exceptions to the competitive bidding process to prevent rich shipyards from getting richer and the poor shipyards from getting poorer. If we are to strengthen and preserve our broad national shipyard mobilization base, which is certainly the goal of this legislation, then it will do no good to allocate contracts for these ships without taking these points into consideration.

Finally, the bills are missing the necessary oversight and regulatory provisions to ensure that the taxpayers' money is being spent wisely and under the strictest controls. Open-ended funding is unlikely to help anyone, and it will certainly not encourage productivity. In fact, any high revenue-dependent program implemented today, with the deficit crisis staring us in the face, should certainly have a clear regulation of funds.

These drafting weaknesses can be corrected; they are not an insurmountable obstacle to the implementation of this program. But they do highlight a critical point I would like to make. A program as broad in scope as build and charter needs to be looked at very carefully by all elements of the maritime industry. It cannot be implemented in haste, for what this program could do—particularly if the Seamen's Wage Adjustment Program is eventually included—is revamp 50 years of American maritime policy in a single blow.

Success will only come if we devise a solution that is fair to all segments of the industry and a solution that is better than what we have today. These proposals contain elements of such an outcome, but we are still, in all frankness, Mr. Chairman, well short of where we must go.

Mr. Chairman, there were two additional things touched on today that I would like to comment on, although I had not prepared to. One is the passenger ship issue which has been raised once again. This is an old, bitter wound in this industry. The industry has been trying to work together very closely. We have been very successful with our cargo preference compromise. I do not think this is the time or the place to inject the passenger ship issue again, because all I see it doing is creating more problems, opening old wounds, and certainly not assisting us in our common goal of working together, because this union still has its original position. We intend to stay with our position on the passenger ship bills, especially the Cunard bill as it was presented before. And we just think that it will do no good, instead of doing some good.

There was another issue mentioned, which was the SWAP program, Mr. Chairman. I thought we were only going to cover two bills, but maybe I will make just a couple of comments on that program if you will bear with me.

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I say that although the word "seamen" appears in the title, let me assure you that no seamen participated in any of the deliberations leading to its drafting. In fact, SWAP was created in a partial vacuum. Only the American liner companies have been involved in its creation. Labor was not invited to the table, nor was the Congress or MARAD. Thus, even though we may be talking about a complete rewriting of our maritime promotion laws and program, several key players in that process so far have been purposely excluded.

I have only seen rough drafts of the yet-to-be-finalized SWAP proposal. I presume that this committee has seen the same draft. And I further presume that members of this committee have been lobbied to support SWAP, as I have.

Mr. Chairman, I remain to be convinced that SWAP represents good maritime policy and good public policy. To date, I am convinced of only one thing. SWAP is a classic pig in a poke. I would urge careful scrutiny to find out precisely what is presiding in that poke. I have had a brief look inside and I don't like what I see. In its most basic context, SWAP is an ODS program with no strings attached. In 1936, the Congress created the subsidy program with some very important strings attached. These strings were designed to permit the abuses born out of earlier subsidy programs. They were designed to ensure fair competition, to prevent new market entry, to prevent bleeding-off taxpayers' dollars to foreign interests, to preserve a fair separation of the domestic and foreign trade operators and, most important, to assist American workers to maintain a fair standard of compensation in the face of abusive foreign competition.

I realize that times have changed, and with that so has the maritime industry. I also realize that this adminstration and recent Congress' have moved to deregulate many American industries. But these moves came only after intensive public debate, careful analysis, and even today we are beginning to rethink the wisdom of some of these actions.

SWAP, as presently conceived, would turn that maritime program on its head. It would scrap the key ingredients of the 1936 act and it would nearly totally deregulate the liner industry with regard to our promotional programs.

I do not believe anyone has examined this concept in any detail, except perhaps to calculate the short-run windfalls a few companies would hope to realize. I urge this committee to step back, slow down, and critically evaluate SWAP and its long-run impact.

You may not like what you see—so far, I know that I am troubled by it.

Mr. Chairman, I thank you for this opportunity. I stand ready to work with you and your colleagues to achieve the goals that every one of us share—a strong and efficient maritime industry, prepared for war, but working in peace.

Thank you very much.

Senator STEVENS. Senator Gorton?

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Senator GORTON. No questions.

Senator STEVENS. Senator Inouye?

[Pause.]

Senator STEVENS. Did you have a statement you wish to make?

Mr. PATERSON. Senator Stevens, Senator Inouye, and gentlemen, I am somewhat chagrined in that the operating exigencies of Eastern Air shuttle got me here too late to review the subjct matter with my legislative representative, Tal Simpkins.

I would simply say that on behalf of the National Maritime Union, we appreciate the offer to appear here, and that I have listened to my colleagues, Frank Drozak and Gene DeFries, and they have in fact said it all. We, too, are prepared to work with this committee, and we second the motion just made by Mr. DeFries.

Thank you.

Senator STEVENS. Thank you very much. Sorry to have not called on you.

Senator Inouye?

Senator INOUYE. Thank you, Mr. Chairman. I would like to note for the record that we have with us the successor to our dear distinguished friend, Jesse Calhoun; Mr. DeFries was recently elected to the presidency of the National MEBA. I would like to congratulate you and welcome you to your first hearing before this committee. You did a good job.

Mr. DEFRIES. Thank you very much.

Senator INOUYE. So that we are aware of the problem we are facing, we ought to consider the present state of maritime labor. In December of 1951 there were over 2,000 active ships in the U.S.-flag fleet, offering over 100,000 billets.

Now, June 1, 1985, there are 409 active ships in the fleet, with less than 16,000 billets. Something has happened on the way to the decade of the 1980s.

Mr Drozak, in your statement you used the word "employer multiplier." Do you believe that this program would create an employer multiplier?

Mr. DROZAK. Most definitely.

Senator INOUYE. I have several questions, Mr. Chairman, I would like to submit. But before I do, I note that in just about every hearing we have had on proposals to improve our fleet, for many reasons, most if not all witnesses have concentrated on their opposition to proposals. I can understand why.

Have any of you drafted any program that you believe would improve the quality of our U.S. fleet?

Mr. DROZAK. Well, Senator Inouye, there have been many proposals drafted by this group sitting here; surely by the SIU, by MEBA and certainly by the NMU. I don't know whether we have ever been able to agree, and that gets back to what I had hoped would be a new day for all of us—that we can agree on something positive. And I would certainly hope that the shipowners and operators would certainly agree on something positive, because if not we are never going to get anyplace.

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My suggestion has been—and I strongly believe in this—I think that this committee should take the ball and run with it. You have had enough evidence presented in testimony before this committee and also the House to draft 900 pieces of legislation. And although speaking only for myself I would accept and support this committee's recommendation. I say this because we are not going to get an agreement with everybody in this room, nor with every ship owner or shipbuilder. We have tried and tried and tried.

I would say to you and to the full committee, you give us a proposal; tell us to take it or leave it. Otherwise we are not going to get any meaningful legislative proposal. I am sincere in that; believe me. We have worked hard for the last 25 years to try to develop a maritime program, a maritime policy for this country. The result has been, as you stated earlier, a drop from 2,000 ships and 100,000 jobs in 1960 to 409 ships and 16,000 jobs today. It is evident, therefore, that our ideas and views are not working, not for the benefit of our membership, nor for the national security of this country. So I would strongly propose that this subcommittee. Give us a piece of legislation and tell us that it is, in your opinion, what is best for this industry. Don't let us continue to try to tell you what is good for ourselves or this country. I don't think we know what is best for us, and even if we did, we could never get a consensus. And I am sincere in my views. Good, bad or indifferent, I would support this subcommittee's recommendation. I put my trust in your hands.

Mr. DEFRIES. Mr. Chairman, Senator Inouye, last week I walked into a meeting completely unprepared, and I was supposed to have a paper outlining our ideas of what the industry needs and what we think are some solutions. I had just been put on a committee and I was not aware that a previous committee had agreed to submit such a paper.

I have our people working on it. I think there are a lot of solutions to the problem we have now. I think we have tried to cure them in the past with Band-Aids.

I had all of the MEBA contracting companies in for a meeting yesterday, which lasted a half a day. And what they were looking for was a lot of Band-Aids stuck all over them. And I tried to explain to them that this industry has reached such a point now that Band-Aid surgery is just foolish. It needs some real cures for long-term problems. It is going to take a lot of people working together with a lot of other people to do this.

I think we have got to put aside our petty differences and our special interests and what we may like to have personally. And I am no different from everyone else here. There are some personal things I would like to have, and I think you know that I am prepared in certain cases to set my personal wants aside to work for the good of this industry.

I think if we don't do it this go-around, there may not be a second go-around. This was the message I tried to convey to our companies because this is my 30th year in this industry, and it is the worst I have seen it.

Thank you very much.

Senator STEVENS. Senator Long.

Senator LONG. Could you give me the figures as it relates to your union, how members did you have in 1951, and how many jobs did they have, and how many do you have now?

Mr. DROZAK. In 1951, 35,000 members.

Senator LONG. 35,000?

Mr. DROZAK. [Nods in the affirmative.]

Senator LONG. How many today do you think you have?

Mr. DROZAK. I have 90,000 in international; but only 9,000 in deep sea. That figure includes the Great Lakes.

Senator LONG. I see. Now, you say you have 90,000 in the international? How do you describe those jobs that are international and not deep sea?

Mr. DROZAK. We have industrial workers, office and clerical workers, heavy machinery, and service employees, as well as professional and Government workers. United Industrial Workers union is a division of the Seafarers.

Senator LONG. Oh, I see.

Mr. DROZAK. Deep sea seafaring, there are 9,000 members, including the Great Lakes; 4,000 jobs.

Senator LONG. And there were 35,000 back in 1950–51?

Mr. DROZAK. Yes.

Senator LONG. How do those numbers compare as far as you are concerned, Mr. DeFries?

Mr. DEFRIES. Senator, they would probably be very similar. We have about 10,000 sea-going members now, not counting shoreside facilities. We had in 1951, we had 99 locals in MEBA. We were a local structure at the time. We had four locals that had 10,000 members. So we have probably same shrinkage in jobs. I don't have the numbers that Frank has.

Senator LONG. How about you, Mr. Paterson?

Mr. PATERSON. We have roughly 10,000 seniority members in the deep sea sector and roughly 3,600 jobs.

Senator LONG. And how many did you have back in 1951?

Mr. PATERSON. In 1951, probably 35, 36,000. Roughly, we have always been equal or just over the membership of the SIU in deep sea sector. We had a lot of passenger ships at that time, and subsequently had a lot of additional jobs.

Senator LONG. I am dismayed to hear that. I know it has been going on, but I am dismayed to hear that because I have a high regard for your union. I think you have done a great job for the country.

Thank you very much.

Senator STEVENS. Any further questions, Senator?

Senator INOUYE. No.

Senator STEVENS. Well, gentlemen, I appreciate your—and I think the whole committee appreciates your offer to work with us. It is the last time in the barrel for all of us.

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I hope that we can find some way to bring these together. And all three of you, SWAP was not part of the hearing. It came up as a legitimate question from my good friend from Hawaii, and I pursued that, too, as something we are going to have to take a look at in the future. But you are right; we have not seen any final proposal on SWAP

Senator INOUYE. Mr. Chairman?

Senator STEVENS. Yes, Senator Inouye.

Senator INOUYE. I was very interested to listen to Mr. Drozak's response. I have kept this to myself, but for some time now I have been working on an omnibus bill. I don't know when I will be ready to present it to you people, but I will see what the reaction is.

However, I am always keeping in mind that when a former colleague in the House, John Murphy, the chairman of the committee there, came up with his omnibus bill. I think just about every member of the industry rolled him over. That was the beginning and the end of his omnibus bill.

Senator INOUYE. I just hope that you fellows would treat my bill a bit more kindly than that.

Mr. DROZAK. Senator, I say this to you in closing. You give us the bill; I will support it. I won't even question it. I put my trust in you.

Senator STEVENS. Senator Long?

Senator LONG. Just to touch on the depth and the extent of this problem, a great deal has to do with the difference between the wage scale here in the United States and the wage scale in these foreign countries, I assume.

Can you give me some idea as to what people are paying for foreign labor out of these ports where it is the cheapest? I guess it would be the cheapest out of a place like Singapore, Hong Kong.

But what kind of wages or foreign labor are being paid compared to U.S. merchant seamen?

Mr. DROZAK Crew costs on a Singapore and Taiwanese vessel run anywhere from $600 to $1,200 a day. That is your Third World crew costs. They can fully crew a vessel for $400 to $1,200 a day.

Senator LONG. I am talking in terms that are a little bit more understandable to the fellow on the street. I mean in term of wages, dollar wages, about how much are they paying per day or per hour for foreign seamen?

Mr. DROZAK. Fifty cents, 75 cents an hour—on up to captain, who may make $400 to $600 a month. But you know, Senator, one of the things that we get confused with, is the standard of living of certain foreign countries. $400 in Singapore is worth the equivalent to what an American seaman would make here if he made $2,000 a month, because his purchasing power in his country is valued a lot more, so his standard is not knocked down to the point to where most people think it is.

If you take the Japanese and European trading nations we are pretty much equal with them with respect to wage levels on board the ships. I know what the Japanese are. We can carry Japanese automobiles on car carriers at the same wage rates as the Japanese.

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Some European countries are in fact a little higher than us. But where the difference comes in is the welfare and pension liability which, as you know, Senator, was severely hurt by the closing of the USPH hospitals.

European governments furnish pension and retirement plans as well as welfare and social benefits at no cost to the operator. That is where the big difference lies. They get benefits from their governments which we do not receive here, and it has to be applied to the ship owner, so automatically those costs create a differential.

Senator LONG. I heard one person suggest the other day that in this country we ought to arrange to phase out all those industries where foreign labor can give an adequate competitive advantage to their industries. And I couldn't help but think that the person saying that I don't think has seen as much as I have seen in the Orient and elsewhere where they have labor available for 50 cents an hour and that type of thing.

Looking at that, one thinks that we ought to just roll over and play dead, whereas they can do it cheaper with foreign labor at 50 cents an hour or even $1.60 an hour. If they have that in mind as a solution to our problem, I don't think they are really realizing the extent or the depth of that suggestion, because a great number of industries, millions of jobs that we would lose, I don't see where we are going to get them back when we sacrifice all those jobs because of low wage scales abroad.

Mr. DROZAK. Senator, I don't think you would get those jobs back if you equal their wages. Even if this country did equal their wages, you would not get those jobs back. Those countries have got a lock on them and it is employment for them. You have millions of jobs that were run out of this country, good industrial-based jobs that were here, such as shipbuilding, steel, auto, et cetera.

And again, you have to look at their standards and what they are provided with by their governments and also by our relief efforts, which we are giving to them, to turn around, to refinance, and then tell us that we have to get competitive with them. It just is not in the cards. The guy that made that statement, Senator, ask him would he like to work for that guy's conditions and benefits here in the United States? Tell him you will hire him right now; at least I will hire him.

Mr. DEFRIES. Senator, if I may add just one thing. One of our companies who had some interest in foreign-flag ships was telling me the other day, in Sri Lanka they can get a stewards department for subsistence. That is their crew cost on it. There is no way in the world this country will ever compete with that.

I think the unions have all been very responsible in the last several years on rollback of wages and cutting benefits, and we are looking forward to the day within the next year when our pension contribution will be close to zero. It will be a fully funded plan.

So we have worked many years trying to get our fringe benefits and our costs where we will be competitive with the European and the Western world. I think we are just kidding ourselves if we ever think

we are going to get competitive with some of the runaway flag companies where people will work just for food and lodging.

Senator LONG. Thank you very much.

Senator STEVENS. Thank you very much. I think we are going to have to have a followup of this hearing. I would hope it would be another one of our meetings so we could sit around a table and discuss some of the comments that each of you made. It is necessary to get these comments on the record so we have a starting place.

I will be happy to support the Inouye bill if that is what comes out of the discussions. Senator Inouye says 6 years. I think we will both be John Stennis's age by the time he gets around to it.

Mr. DROZAK. Mr. Chairman, we won't be here six years from now.

Senator STEVENS. Well, Danny and I will be. We will be here. We will pursue it, no matter how long it takes. There may be some changes in OMB, too, by that time.

Senator STEVENS. Thank you very much. And we will be happy to have the additional statements if you want to submit them for the record.

Our next representative is William Haggett, chairman of the board, Shipbuilders Council of America, and he is accompanied by Lee Rice, president of the Shipbuilders Council of America.

STATEMENT OF WILLIAM E. HAGGETT, CHAIRMAN, SHIPBUILDERS COUNCIL OF AMERICA; ACCOMPANIED BY M. LEE RICE, PRESIDENT

Mr. HAGGETT. Good morning, Senator.

Senator STEVENS. Good morning, and welcome.

Mr. HAGGETT. My name is Bill Haggett. I am president and chief executive officer of Bath Iron Works, a shipbuilding company in Maine, and I am also chairman of the Shipbuilders Council of America.

With me this morning I have Lee Rice who is president of the Shipbuilders Council, and in that capacity we represent the major American shipyards and principal supplier of materials to those shipyards.

I would like to open by saying that the council strongly supports a build and charter program as the most effective legislative initiative that can contribute to the achievement of vital national objectives, and we support that program without reservation.

We believe that it provides needed, militarily useful ships which can be operated in a commercial environment.

The program will help sustain shipyards, skilled workers and management which is needed as components of the Shipyard Mobilization Base. We believe that the program sustains the pool of U.S. citizens in seagoing positions, and that those seagoing positions will be continually available to a greater degree than presently exists.

And it provides an opportunity to improve the operation of American shipping companies.

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Indeed, of all the witnesses who have appeared this morning, I think we have more in common than is reflected in the differences which we tend to hear.

There certainly has been no debate of the necessity for this nation to maintain an adequate maritime capability. The capability includes diversified shipping assets, required Shipyard Mobilization Base, and sufficient seagoing manpower to enable operation of our ships during a national emergency.

Further, all agree that each of these vital capabilities is experiencing a period of decline, as is reflected from speaker after speaker today. There is no debate, however, as to whether or not the decline of the Shipyard Mobilization Base has reached the point where national security is a real concern.

As professionals who will be called upon to carry out the many and demanding tasks required of our industry in time of mobilization and war, we know that the capability and capacity of the industry have fallen below the level at which we can perform required assignments. Facts which detail the condition of our industry are contained in the attached address to my statement which was delivered by Mr. Rice just recently. In that, he examined the entire broad range of transportation issues.

Sealift and the Shipyard Mobilization Base issues were identified as critical issues of concern. The data presented there show conclusively that there is a significant problem to be solved to maintain America's shipbuilding and ship repair capability.

It is particularly disconcerting to see America's shipbuilding base rapidly eroding at a time when the performance of our shipyards is improving. That performance is improving as a result of technological advances in the shipyards, improved methodology that is being employed, and concessions that have been negotiated with our bargaining groups.

As a result of that, the cost of building ships in this country has decreased, while the quality is improving and adherence to schedules in our shipyards is consistently good. While there is always room for improvement, we can state confidently today that American shipyards can compete for the best in the world in naval construction.

Having reached this point, it is really sad to see American shipyards closing, especially when those closing represent a weakening of our national defense capabilities. Mr. Rice's analysis shows that manpower projected to be in place at the time of mobilization will be less than adequate: in reality, a shortfall of about 25 percent of the required skilled manpower will occur in the near future. Indeed, as of today, that shortfall is over 18 percent: or, to put it in a different way, we lack 30,000 skilled production workers who must be on the job if the mobilization tasks are to be done correctly and on time.

It is not an overstatement to point out that the problem has become critical and that national security is at risk.

The Navy, justifiably, has been focusing its primary concern on rebuilding our combatant Navy. And it is clear that there is a division within the Government as to who is responsible for solving our

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mobilization problem. It is our judgment that the Navy and Department of Defense recognize that the problem exists and must be solved. This legislation before us today offers a vehicle for that solution.

At present, as you, Mr. Chairman, have identified, there exists a unique opportunity to attack this problem. The shipbuilding industry over the past several years has performed with high productivity and below budgeted costs under many of its Navy contracts.

As a consequence, there exists within the Navy shipbuilding budget unexpended funds which have been approriated but are unobligated. You have proposed, together with your colleague, Senator Inouye, that these funds be used to alleviate the problem. We fully agree that that approach is sound, it is fair, and it is fiscally responsible.

There are some who argue that the funds should be used to build Navy ships. That may be a valid statement. But we would like to point out that support for the shipyard mobilization base is most effectively achieved through construction of merchant ships. Substantially fewer funds are available to purchase shipyard services when large amounts of military and weapon-related costs are spent for the construction of naval combatant ships and auxiliaries.

Indeed, only 30 percent of the Navy shipbuilding budget is actually spent in our shipyards, as compared with nearly 100 percent which would flow to the shipyards under a merchant ship build and charter program.

Mr. Chairman, as you know, present policy is that commercial sealift ships are to be provided through support for U.S. liner company operations, with reliance on Jones Act trades and the preference trades. Policy edicts have abandoned U.S. shipbuilder participation in support of the other trades of world commerce. Even a very optimistic projection of the number of ships built for these chosen commercial markets will not provide adequate numbers or types of ships to support national policy, as has been pointed out so clearly this morning by Senator Inouye.

Therefore, without some change in direction, we cannot meet the nation's sealift or shipbuilding requirements. Consequently, the Government has been forced to respond to its minimal requirements by increasing then number of ships under its direct control.

For example, since 1982 the planned Ready Reserve Force has grown from a planned number of 30 ships to a planned number of 110 ships, and the end has not yet been reached. To solve the identifiable shortfall of tankers, we believe that the Ready Reserve Fleet will have to grow to about 150 ships. Expanding the Ready Reserve Fleet, however, causes a surge in workload for our shipyards during mobilization which we do not believe has been factored into our defense planning, nor has the problem of manning the Ready Reserve been solved as the number of available seagoing personnel on commercial vessels continues in sharp decline.

The build and charter program embodied in S. 1833 was crafted to achieve the four objectives which I enumerated earlier—to provide militarily useful operating sealift ships; to sustain the Shipyard

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Mobilization Base; to support the required seagoing manpower needs; and to support ship operating needs, while at the same time not causing unacceptable competitive disadvantage to various sectors of the shipping industry.

We are convinced that the approach is fundamentally sound and that a start, even if it is imperfect, must be made now or unrecoverable loss of time will occur. Then the ultimate cost to solve this problem will be significantly higher.

In our view, the ships constructed under this program will be put to commercial use and should have high military value. We believe that ro/ro ships, combination container-ro/ro ships for trades to the lesser developed countries, product carriers and neo-bulk ships can be built and charted economically.

An objective of the program should be to foster the entrepreneurial development of trades where U.S.-flag operators are not presently functioning effectively. The program should be funded, we believe, over the next several years if it is to succeed.

We cannot predict with great precision the circumstances that will exist by the end of this decade when ships are being delivered. It is our expectation, however, that the need for additional sealift assets, continued support of the Shipyard Mobilization Base, and sustaining the seagoing manpower base will remain national concerns even if the build and charter program has met its objectives.

We believe that the program should be funded as a Navy program and managed by the Navy, even though the ships are built to commercial standards, and that is necessary if it is to achieve its objectives.

Furthermore, we are convinced that other than the sale of vessels, there must be complete flexibility as to the terms under which the ships can be chartered if the goal of developing new shipping markets is to be achieved. Other approaches to build and charter may work. We remain convinced that the approach which we have proposed is workable and offers good solutions to the various and difficult problems before us.

But we are prepared to consider seriously any other meaningful alternative.

We also commend you and the subcommittee for undertaking the development of this legislation and pledge our support and active efforts toward enactment.

And I would like to make just one more observation before concluding. As I reflect back on positions that shipbuilders and the Shipbuilders Council have taken over many years, I recall very well the hard, strong positions that we have taken in support of our selfish needs as an industry and the opposition that we have put forward to offset any compromises to what we viewed selfishly as essential to shipbuilders.

My firm belief is that over the past few years we have changed our view of the world, and that we do recognize that compromise is important in terms of working toward a solution, and I believe that the shipbuilders in this country and the shipbuilding industry, as

represented by the Shipbuilders Council, is prepared to work with the other interests in this industry, and I am certain that we are prepared to work with you and the Congress to come to a program that achieves the fundamental objectives that I defined earlier.

Thank you.

Senator STEVENS. Mr. Rice, do you have any comments this morning?

Mr. RICE. No.

Senator STEVENS. Senator Gorton?

Senator GORTON. No.

Senator STEVENS. Senator Inouye?

Senator INOUYE. Thank you, Mr. Chairman.

Do you have any views on the so-called Bentley bill introduced by Representative Helen Bentley in the House of Representatives, a bill that provides for the construction of the hull and propulsion system of passenger cruise vessels in American yards, and the hotel portion in foreign yards?

Mr. HAGGETT. Senator, I will ask Mr. Rice to respond to that. I am sure he is more familiar with the bill than I am.

Mr. RICE. The Shipbuilders Council has not taken a position on that bill. It is, as you know, supported strongly by one of our members with the belief that that is the only practical way to build a passenger ship in the United States, to allow a very significant part of so-called hotel work to be done abroad.

As I said, we do not have a Council position on it.

Senator INOUYE. Thank you.

Senator STEVENS. I am sure you realize that part of the concept involved here is that if we have a build and charter program, that we will consider a window for some type of foreign-built acquisition by some of the operators involved.

Are you aware of that? Do you consider that as being a fair balance?

Mr. HAGGETT. Senator, that is a very good example of the type of movement that I think we have made in our industry. Five years ago we would have been adamantly opposed to foreign construction of any type. Today I think the reality is that we would have to consider a reasonable program, and it is not unrealistic that there should be needs for foreign construction at some level or some type, and while we are not promoting construction of ships in foreign countries, I think it is going to be part of any solution and we are prepared to sit and listen and talk to you and others in the industry along those lines.

Senator STEVENS. Thank you very much. That is representative of a good attitude in the industry. We do appreciate it.

Thank you, gentlemen.

We will have the next witness, Philip Shapiro, the Vice President and General Council of the Apex Maritime Corporation, discussing tanker and bulk carriers. And he is accompanied by Mr. Tom Mills.

Good morning, Mr. Shapiro.

STATEMENT OF PHILIP J. SHAPIRO, VICE PRESIDENT AND GENERAL COUNSEL, APEX MARINE CORPORATION; ACCOMPANIED BY THOMAS L. MILLS, COUNSEL

Mr. SHAPIRO. Good morning, sir. How are you?

Mr. Chairman, Senator Inouye, I am Philip Shapiro, Vice President and General Council of Apex Marine Corporation which operates 18 U.S.-flag vessels in domestic and foreign commerce and has three vessels under construction for delivery and documentation under U.S.-flag.

Captain Leo V. Berger is the principal owner of the companies which own the vessels which Apex operates. These companies are collectively known informally as the "Berger Group."

Indeed, we are grateful for the opportunity to participate here before you today. We wish to compliment Senators Stevens and Inouye on developing a program to support the U.S.-flag merchant marine engaged in foreign commerce and in general, subject to a few comments, we wholeheartedly support the effort presented by this legislation.

It is vitally important to our company that vessels built under this build and charter program be strictly limited to sale or charter at prices or charter hire reflecting nothing less than the world price for new construction for the same vessel at the time the vessel is delivered from a U.S. shipyard.

Our companies have made very substantial capital investments in vessels for the foreign commerce of the United States, principally in the cargo preference trades. We cannot afford to see that investment undercut by new ships constructed or chartered at less than the world price of constructing a new vessel.

Accordingly, we recommend that in S. 1832, the committee delete the following language from line 8 through line 10 on page 3: "taking into account financing terms and relative delivery times available from U.S. and foreign shipyards."

It would be virtually impossible to translate accurately financing terms and delivery times into reduced capital costs. We fear that in its enthusiasm to charter these vessels, the Navy may reduce the charter price significantly to account for such amorphous conditions.

In addition, since the Navy is building the vessels and designing the vessels, there is really no delivery period. The purchaser will presumably be buying a shelf item from the Navy. Since financing terms are not available under the statute, the company purchasing the vessel would be free to obtain whatever market financing terms were available to him.

In addition, we suggest that in S. 1832, section 1401(d) beginning on line 23 of page 2, the period be changed to a comma, and the following language be inserted: "but in in no event for an annual charter hire equal to less than 16½ percent of the foreign cost of constructing the vessel in a foreign shipyard at the time the vessel was delivered to the Secretary."

The same language should be inserted at the end of section 1401(d) in S. 1833 beginning on line 8 of page 3 where the period should be changed to a comma and the quoted language thus inserted.

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The 16½ percent is intended to represent a 4 percent annual depreciation charge and a 12½ percent annual interest. When a vessel is chartered to an operator, it amounts in effect to the loan of the capital asset and the bareboat charter hire should at least reflect the annual depreciation on the asset, plus an interest factor for the loan of its capital value. The 4 percent represents annual depreciation based on a 25-year life and 12½ percent is an estimate of the long-term interest rate which would be applicable under title XI financing or similar financing.

Moreover, the supervision of and actual choice of a particular vessel's design should be reserved for the industry's private sector, who are knowledgeable of the commercial requirements needed to ensure the competitiveness of each vessel in its eventual trade.

We are, of course, mindful of the necessity that these vessels be militarily useful. However, our companies, as well as other U.S.-flag operators, have constructed U.S.-flag vessels in foreign shipyards under section 615, incorporating those essential national defense features in the most modern, efficient and competitive vessels afloat today.

With these modifications, our companies wish to lend our support to the efforts of this committee to take one step toward rejuvenating the American merchant fleet engaged in foreign commerce.

Thank you very much.

Senator STEVENS. Those are very constructive comments, and we will be glad to take a look at them. I will have to think about them for a while. My colleague will, too. But we appreciate the manner in which you have approached this legislation.

Senator Inouye?

Senator INOUYE. I am just intrigued by the 16½. I think that is probably realistic.

Senator STEVENS. It is. It is a most interesting suggestion, that there be a floor there that represents some kind of basic equality. That is a good suggestion; we will take a look at it.

Mr. SHAPIRO. Thank you very much.

Senator STEVENS. That is the last witness we had scheduled for today. Senator Inouye and I will discuss this with our staffs and analyze the comments that have been made. It would be my hope, and I think my colleague from Hawaii joins in this hope, that before the month is out we could have another industry meeting to sit around the table and discuss this concept.

The defense bill will not be before the Senate until after Thanksgiving, so we have adequate time to discuss this prior to action by the Senate on the reprogramming of the funds that are in the naval account already.

And I would hope that all concerned would examine the comments made by other portions of the industry. We have available copies of the statments made, and we would look forward to any suggestions you might have as to how to work out the various problems that are obvious from testimony that was presented.

But overall, I want to say I am encouraged by the approach and I particularly thank you all for being constructive in trying to analyze a most difficult set of problems.

Senator Inouye?

Senator INOUYE. I just wish to associate myself with your remarks.

Senator STEVENS. Thank you very much. Thank you all.

[Whereupon, at 12:42 p.m., the hearing was adjourned.

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ESTABLISH A BUILD AND CHARTER PROGRAM

THURSDAY, MARCH 20, 1986

U.S. SENATE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
SUBCOMMITTEE ON MERCHANT MARINE

Washington, D.C.

The subcommittee met, pursuant to notice, at 2:00 p.m., in room SR-253, Russell Senate Office Building, Hon. Ted Stevens (chairman of the subcommittee) presiding.

OPENING STATEMENT BY SENATOR STEVENS

Senator STEVENS. Thank you all for coming. I want to state in the beginning that my good friend, Senator Inouye, has had a personal situation develop and he cannot be here. I am going to put his statement in the record following mine. I know he has a deep interest in the subject.

On November 15, 1985 this subcommittee held a preliminary hearing on the Mariner Fund concept. Many representatives from the Merchant Marine industry testified in support of the basic concept, but questioned the provisions included in prior legislation. As a result of that hearing, I introduced S. 1885 that would establish a revolving fund for the purpose of constructing commercially useful vessels with high military value.

Four separate committees will review the merits of the proposed program before an authorization can be approved.

In addition to this Commerce Committee review, the Senate Armed Services has requested a referral of S. 1885 prior to any action on the floor. The House Merchant Marine and Fisheries Committee and the House Armed Services Committee have already held hearings on the Mariner Fund concept.

The purpose of this hearing is to determine how the Mariner Fund could be implemented, assuming authorization legislation is passed. We still have questions relating to implementation, including the type of vessels which could be built under the auspices of the fund, the existence of overtonnage if any, the appropriate role of the Maritime Administration in the consultative process and whether there is interest on the part of carriers to charter or sell the type of vessels necessary to enhance sealift capacity.

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I know the administration formally opposes the Mariner Fund for budgetary reaons and we are going to hear that today, I am sure. However, the Strategic Sealift Program is already recognized as an essential component of our defense force. The Mariner Fund provides a cost-effective supplement to the existing sealift enhancement effort in my judgment.

The Federal Government will receive a return on its investment from charter fees. The companies which charter the vessels would assume all maintenance costs, thus offsetting the cost of maintaining the ready reserve fleet.

[The statement follows:]

OPENING STATEMENT BY SENATOR INOUYE

As the subcommittee continues its efforts to recommend legislation to implement a build and charter program, I wish to commend my chairman for his leadership. Because of his initiative Congress has already appropriated $852 million for this program, contingent upon enactment of authorizing legislation.

At the conclusion of our earlier hearing on this subject I said that I believed the solution to some of our maritime problems could be found within this hearing room. If there were ever a doubt that industry unity is essential to any legislative solutions of its problems, I believe that doubt will be put to rest by what happens here.

If we can reach a consensus on a realistic build and charter program, we will be well on the way because a major obstacle—funding—was moved last December when Congress appropriated $852 million.

If, on the other hand, support for build and charter legislation is conditioned upon other controversial proposals, then we will be back to "square one," in my judgment. Only this time "square one" will not only mean a "stand-off" among the various maritime interests, but the loss of $852 million.

So the opportunity is here, and I would hope the industry helps us take advantage of it.

Senator STEVENS. I know our first witness has been across this road before, so Mr. Secretary, we are happy to have you here and would be pleased to have your comments.

STATEMENTS OF EVERETT PYATT, ASSISTANT SECRETARY, SHIPBUILDING AND LOGISTICS, DEPARTMENT OF THE NAVY; JOHN A. GAUGHAN, ADMINISTRATOR, MARITIME ADMINISTRATION, DEPARTMENT OF TRANSPORTATION; ACCOMPANIED BY RICHARD E. BOWMAN ASSOCIATE ADMINISTRATOR FOR MARITIME AIDS; AND REGINALD A. BOURDON, ASSOCIATE ADMINISTRATOR FOR POLICY AND INTERNATIONAL AFFAIRS

Mr. PYATT. Thank you, Mr. Chairman.

Senator STEVENS. Pardon me.

And then we will listen to Mr. Gaughan, and I understand that you are accompanied by Mr. Bowman and Mr. Bourdon. If either of you have any comments we would be happy to listen to you, too.

Thank you.

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Mr. PYATT. I would like to submit my statement for the record and briefly summarize, because I know you have questions you would like to raise.

You understand properly the administration is opposed to this legislation because they believe that it is not necessarily the most efficient way to buy ships, to acquire ships for sealift. We believe that many of the ships that would be purchased under this kind of program are not likely to be economically viable and to provide a sufficient return on the government's investment to truly make this fund a revolving fund.

Therefore, long-term viability would require continuing annual appropriations by the Congress. In looking at the current situation, we believe there is only one type of ship likely to be built, and that would be product carrier and tankers. We have recently completed the DOD Sealift Tanker Study which shows a shortfall of about 75 handy-size tanker equivalents.

We have asked U.S. owners to offer product tankers in the Navy's 1986 RRF procurement and got very few, no responses rather. So this appears to be the only commercial segment which is not overtonnaged and in fact it is fully employed, although the rates that they can charge are pretty skimpy as such.

Chartering these government-built tankers for commercial use may be a feasible way, if we are willing to accept a charter hire so low as to offset foreign flag advantages such as lower crew cost, but with this limited application I think it is unlikely that the Fund could be made to truly revolve.

That completes my prepared statement.

[The statement follows:]

STATEMENT OF EVERETT PYATT, ASSISTANT SECRETARY, SHIPBUILDING AND LOGISTICS, OF THE NAVY DEPARTMENT

Mr. Chairman and distinguished members of the Committee. I am Everett Pyatt, Assistant Secretary of the Navy (Shipbuilding and Logistics).

It is my pleasure to appear before this committee to discuss S. 1885, a bill which would establish a "Military Auxiliary Revolving Fund."

This revolving fund would be used by the Navy to build militarily useful merchant ships and charter or sell those ships to private operators for use in commercial trades. The FY 1986 Continuing Resolution has earmarked $852 million in prior year Navy shipbuilding savings as the initial capital for the fund.

Mr. Chairman, we are opposed to this legislation.

The build and charter method of procuring sealift capability is not necessarily more cost-effective than our current method. Our principal program for increasing our defense sealift capability involves procurement of existing militarily useful ships that have become surplus to commercial requirements. Those ships are placed in the Ready Reserve Force (RRF), where they can be activated for use in emergencies.

We also believe that many types of vessels constructed under a build and charter program would not be commercially viable unless the charter rate or the sale price were extremely low—too low to permit recovery of the government's investment over the life of the ship. This would mean that the revolving fund could not be replenished from the proceeds of charters or sales. Long-term viability of the program would require continuing annual appropriations by the Congress.

The bill under consideration has problems in its detail. Specifically, the procurement process specified will not work. It contemplates a two-step process—first, competition for construction of a ship, then competition for chartering the ship. We believe that ships should not be built on speculation. If a build-and-charter program were instituted, it should be designed so that shipbuilders and ship operators presented proposals for construction and charter operation. This would prevent construction of ships for which there was no market. It does not make sense to build ships that would go directly into Ready Reserve Force inactive status.

The only ship type we would likely build under this program would be product tankers. The recently completed DoD Sealift Tanker Study shows that, in 1990, we will have a capacity shortfall of about 75 handy-size tanker equivalents in our sealift tanker fleet. We asked U.S. owners to offer product tankers in our FY 1986 RRF procurement. No responses were received. This appears to be the only commercial shipping segment which is not overtonnaged and, in fact, is fully employed. As such, chartering of government-built tankers for commercial use may be feasible if we are willing to accept a charter hire rate low enough to offset foreign-flag advantages such as lower crew cost.

Mr. Chairman, we are in accord in our goal—a strong, healthy U.S. merchant marine and shipbuilding industry. We do not believe, however, that the proposed build and charter legislation will accomplish that goal.

Thank you for this opportunity to present our views. I would be pleased to answer any questions you may have.

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS

Question. One witness (APEX Marine) this morning will state that it is his understanding that under S. 1885, "the Navy will build the vessels and design them: and therefore any commercial charterer or purchasers will presumably be buying a shelf item from the Navy."

At our earlier hearing, however, the same witness said that "supervision of and actual choice of a particular vessel's design should be reserved for the industry's private sector, who are knowledgeable about the commercial requirements needed to ensure the competitiveness of each vessel in its eventual trade."

Another witness (Shipbuilders) will testify that it is his understanding that the Navy would engage the Maritime Administration as it procuring and chartering agent.

What are your views about the proper division of authority with respect to the choice of the type of vessel, its design, etc.; and should S. 1885 spell out in more detail who has the say about what, as among the Department of the Navy, MARAD, and prospective charterers or purchasers?

Answer. We have not considered the structure for implementing this legislation. However, since Navy funds are proposed to be used for militarily useful ships, we

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believe that authority for all aspects of such a program should reside with the Navy.

Question. A recent news article (Journal of Commerce, February 28) reports that: "The Army's traffic managers think containerships aren't that great for military cargo; and that the Army's Military Traffic Management Command doubts that more than 20% of military cargo could be carried on containerships in an emergency."

Inasmuch as vessels built under the build and charter program must be militarily useful, does the assessment of the army's Military Traffic Command mean that few, if any, containerships would be built under the program?

Answer. First, it should be noted that our programs to procure SEASHEDs and flatfracks are designed to make containerships militarily useful. Also, containerships can carry containerized military resupply items.

Since the U.S. dry cargo merchant fleet is expected to contain adequate containerships for use with or without SEASHEDs and flatracks well into the future, that type of ship could be expected to be low on any build and charter priority list.

Question. In earlier testimony before the Subcommittee you said the charter hire or sale price would have to be extremely low if the vessels were to be commercially viable in international trade; and as a consequence the revolving fund would stand little chance of self-replenishment.

That assessment would not be accurate for passenger cruise vessels built under the program would it? I mean those vessels would operate in the Jones Act trades which are protected against low cost foreign-built vessels.

Answer. We are not interested in building passenger ships since they have low military utility.

Senator STEVENS. Mr. Gaughan

Mr. GAUGHAN. Thank you, Mr. Chairman. Mr. Chairman, I would also like to submit my statement for the record.

In November, when Mr. Marquez, the General Counsel, testified on the predecessor build and charter bills, he indicated that the Department favored the approach that we had offered in the form of promotional legislation to authorize foreign building Build Foreign and immediate eligibility. That remains our view, sir.

So I regret to inform you that we cannot support S. 1885 for the reasons that we stated last November. I am prepared, with my colleagues, to answer any questions you might have.

[The statement follows:]

STATEMENT OF HON. JOHN A. GAUGHAN, ADMINISTRATOR, MARITIME ADMINISTRATION

Mr. Chairman and Members of the Subcommittee on Merchant Marine. My name is John A. Gaughan and I am the Maritime Administrator of the Department of Transportation. I am pleased to appear before the Subcommittee to present the views of the Administration with respect to S. 1885.

S. 1885 would amend the Merchant Marine Act, 1936, as amended (46 App. U.S.C. et seq.), by the addition of a new Title XIV—Build and Charter.

Mr. Chairman and members of the Subcommittee. On November 15, 1985, Jim J. Marquez, General Counsel of the Department of Transportation, appeared before this Subcommittee to present the views of the Department on S. 1882 and S. 1883, the predecessor legislation to the bill under consideration this afternoon. Then the Department could not agree that build and charter was the correct approach to support the U.S.-flag Merchant Marine, and opposed S. 1832 and S. 1833. Instead, we viewed legislative proposals submitted by the Administration and introduced by the Chairman as S. 1481 and S. 1482 as the appropriate approach. As you know, pursuant to those bills, the Secretary of Transportation would authorize subsidized U.S.-flag operators to construct, reconstruct, or acquire vessels outside the United States with eligibility to participate in certain promotional programs.

The Department favored the approach taken in S. 1481 and S. 1482 because it is consistent with Administration policy that the expense of a modern commercial fleet should be borne by the private sector and not the taxpayer. In contrast, we believed that under the build and charter or sale program provided by the predecessor bills, S. 1832 and S. 1833, the purchase price or charter hire would have to be so low, in order to be commercially viable, that it would require annual appropriations, in addition to the $852 million proposed in 1986, in order to continue the program. I regret to inform you that the Administration cannot support S. 1885 for the same reasons we could not support the predecessor legislation last November.

Mr. Chairman, we continue to deeply appreciate your efforts to support the U.S.-flag merchant marine.

That concludes my prepared statement. I will be pleased to answer any questions that you or the Members of the Subcommittee may have. Thank you.

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Senator STEVENS. Well, I know that you all have been over this subject in House hearings. What really is your answer to those of us who question the adequacy of the Ready Reserve to meet emergency wartime needs?

Mr. PYATT. Well, I think the issue on adequacy is built around the avaiability of people, and I believe the ships that are there would be available, would be available on the time scales we have talked about, from 5 to 30 days; and in the current environment, from what we can tell, there would be adequate people to man those ships.

If the Merchant Marine continues to decline, you could run into more problems on the financial side. It is clear that if you could have a ship assigned to the Ready Reserve and operating, you avoid the cost of the million dollars per year of taking care of the ship, and you should be able to generate some revenue in fact to offset—rather, to provide a positive cash flow.

So that is the way I kind of summarize the manning and the financial aspects.

Senator STEVENS. Have you ever looked at the Civil Air Reserve Fleet with respect to the availability and readiness of airlift and compare it to that of the Ready Reserve Fleet?

Mr. PYATT. Well, an airplane is more mobile than a ship and so I have a little trouble with how quick you can bring it to use. When we tried to plan sealift enhancement features in the Navy's program we copied after the concept of the CRAF. I had worked on the CRAF before in previous work, and so we tried to copy some of the concepts.

Senator STEVENS. But it did not come through very well. The Civil Air Reserve Fleet is out there working. The Ready Reserve Fleet is tied up at the dock, costs us $100 million a year, and is not available for emergencies.

I understand where you are coming from on a budgetary standpoint. I do not understand why your opposition to the bill is based on nonbudgetary terms. I think that is the main problem we have.

Mr. PYATT. The issue on the CRAF-like resemblance, we have funded in the Navy budget, in the Defense portion of the budget, improvements for the container ship portion of the merchant fleet to make it look more like the CRAF. We did copy that and are trying to get it implemented this year, in this year's appropriation. That is where it stands.

Senator STEVENS. Mr. Pyatt, what do you think should be done to meet the needs of the civilian portion of our economy during wartime? We really do not have an active Merchant Marine that we can call upon in the event of emergency today operating under the U.S. flag.

Have you done anything to compare emergencies in the past, the number of ships that were available at that time and how fast they were made available to us with the situation today in terms of what could be made available in the event of a real emergency?

Mr. PYATT. I did not bring the numbers with me, but generally the comparisons that we have done in the Defense Department show that the number of ships is substantially down from the past. The capacity is

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down a little bit because they have gotten larger. The question that you get into is, can you distribute the ships properly around the world to do the things you want to do in the time scale that you need to?

Our last study of sealift showed that we were marginally inadequate, I believe was the phrase that was used just on the short side. Since that study was developed, the U.S. Merchant Marine declined at a faster rate than initially projected, and so that estimate would be on the lower side of where we stood before.

So, yes, there is a problem. It could be a growing problem. That is the reason the U.S. Navy got into the sealift business about 4 years ago for the first time.

Senator STEVENS. Well, let us just assume for the purpose of discussion that we obtained a substantial agreement from the Soviets in terms of the arms control negotiations that are going on now and that we then faced the question of defending the country in a near-conventional mode.

Do you think we have the sealift capacity to be engaged in conventional defense of our intersts around the world?

Mr. PYATT. Alone? Without participation of our allies?

Senator STEVENS. We have been alone in most instances recently, Mr. Pyatt.

Mr. PYATT. The reason I asked the question was, in one instance, we have looked at involvement alone in the Middle East and in that instance, the sealift was adequate. Alone, we could not sustain Middle East plus Europe. We require European participation.

We could not sustain another theater outside that without other Allies' participation.

Senator STEVENS. Well, even if, God forbid, we had to find ways to move troops to Central or Latin America, how many troop ships do you have available right now on 5 days' notice?

Mr. PYATT. None as far as I know. We have amphibs available. That would be the first movement, I would assume. And the rest would have to move by air to a local area and then be transported.

Senator STEVENS. Mr. Gaughan, you say that you would like to see the needs met by virtue of Build Foreign; is that right?

Mr. GAUGHAN. That is correct, Mr. Chairman.

Senator STEVENS. In your judgment, if you have you made any conclusions, what would that do to the remaining shipbuilding capacity we have in the country?

Mr. GAUGHAN. Mr. Chairman, when you look at the vessels that are currently of commercial utility to U.S. operators, they are typically the type of vessel that falls, first of all, on the lower end of the scale of what the Navy looks for in terms of military need. The capital cost and the construction times involved have made it quite clear that operators, although they might wish to build in this country, simply are not economically able to build in this country and then compete because of the higher capital cost.

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Senator STEVENS. Well, I think that is probably a correct statement of the situation, but isn't there a need for shipbuiding capability to be maintained in this country?

Mr. GAUGHAN. There most certainly is, Senator.

Senator STEVENS. Do you think we are going to get that solely by naval expenditures?

Mr. GAUGHAN. Sir, I think the particulars are probably best answered by the Navy, but it is my understanding that based on studies in which we have participated with the Navy, that there is the view that the shipyard industrial base is adequate through 1988, I believe is the year, and beyond.

Senator STEVENS. Will MarAd have any role in trying to solve the problems of our U.S.-flag Merchant Marine if this bill is enacted? What is your role right now?

Mr. GAUGHAN. Under the legislation as introduced, we do not have an active role in the Mariner program, Senator.

Senator STEVENS. I understand that, but you are opposing this legislation. I assume you agree that there is a problem in not having U.S.-flag vessels that are capable of meeting our civilian needs during emergency which operating under U.S.-flag and subject to requests from the government to assist in maintaining our commerce.

Mr. GAUGHAN. Yes, sir.

Senator STEVENS. If you do not support this bill, what do you support to help meet those needs?

Mr. GAUGHAN. Again, Senator, the legislation that would allow foreign building and immediate eligibility to carry preference cargo for reflagged vessels along with our existing ODS program and our marketing program, sir.

Senator STEVENS. Let us put it this way: I do not know if you have one—I would like to see a chart of the comparison of the number of vessels operating under the U.S. flag with the inception of the ODS program and to really see what ODS has done to maintain the U.S.-flag operations.

This could entail a comparision of the number and cost of the ships at inception and the number and cost of ships which we have now.

Mr. GAUGHAN. Senator, if I could, I would provide that for the record. But certainly I think it will show that the program has not been as successful as may be envisioned.

[The following information was subsequently received for the record:]

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U.S.-FLAG FLEET COMPARISON

Year	No. of vessels under ODSA	Percent of fleet	Unsubsidized foreign trade vessels	Percent of fleet	Jones Act vessels	Percent of fleet	Total U.S. flag fleet
1956-60	1,527	29	1,667	32	1,915	39	5,109
1961	312	32	298	30	363	38	973
1962	313	31	366	37	306	32	985
1963	316	32	353	36	305	32	974
1964	318	33	359	37	286	30	963
1965	311	32	365	38	272	30	948
1966	307	31	411	42	247	27	965
1967	313	32	411	42	250	26	974
1968	307	31	418	43	242	26	967
1969	288	30	396	42	247	28	931
1970	270	30	261	32	262	38	793
1971	206	28	269	37	236	35	711
1972	210	32	217	33	224	35	651
1973	179	30	214	35	203	35	596
1974	174	29	184	31	225	40	583
1975	190	32	197	33	193	35	580
1976	194	33	184	31	199	36	577
1977	187	32	144	25	240	43	571
1978	186	31	164	28	234	41	584
1979	177	31	168	29	224	40	569
1980	163	28	164	28	251	44	578
1981	177	30	150	26	247	44	574
1982	173	30	171	29	229	41	573
1983	175	32	153	28	210	40	538
1984	169	34	145	29	178	37	492
1985	147	30	144	30	186	40	477

Notes: Figures include freighters, bulk carriers and tankers.
Figures exclude Great Lakes vessels and vessels of less than 1,000 tons deadweight.

ODS PAYABLE BY YEAR

Year	No. of vessels under ODSA	ODS payable for year
1956-60	1,527	$687,674,698
1961	312	168,841,513
1962	313	174,467,393
1963	316	190,535,793
1964	318	219,660,312
1965	311	182,899,231
1966	307	199,504,598
1967	313	215,416,871
1968	307	219,189,180
1969	288	228,038,947
1970	270	234,449,812
1971	206	205,261,360
1972	210	190,732,158
1973	179	219,475,963
1974	174	219,297,428
1975	190	260,676,152
1976	194	275,267,465
1977	187	294,779,691
1978	186	285,075,424
1979	177	279,347,897
1980	163	385,399,792
1981	177	350,299,767
1982	173	364,833,552
1983	175	275,821,894
1984	169	338,798,000
1985	147	329,999,207
Total ODS paid 1956-85		6,995,735,098

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Senator STEVENS. Not only not been as successful; it has probably been the most costly failure in the history of the Merchant Marine. I just particularly feel like in shipbuilding, it is just not there.

It is unfortunate. I think everyone concerned is trying to work and find a way out of the current problems, but I think as I said at the beginning, that you all have been around this and down this road in the House. I do not see any reason to belabor the issue today.

We are still going to keep trying and see if there is not some way that we can fit all these pieces together and work out something that would be acceptable to the administration, even minimally so.

It would still be, I think, a step in the right direction to try to save the U.S. Merchant Marine before we are all invited to the funeral.

We appreciate your courtesy in coming. Thank you very much.

Mr. Bourdon, Mr. Bowman, I do not think we need to belabor our differences at this point.

Mr. PYATT. Thank you, Senator.

Senator STEVENS. Our next witnesses, Mr. Amoss, chairman of Lykes; Mr. Lowman, chairman of Farrell; and Mr. Skouras, president of Prudential.

I do not know whether this is the way this is listed on our list is the way you would like to proceed.

STATEMENTS OF W. JAMES AMOSS, JR., CHAIRMAN AND CHIEF EXECUTIVE OFFICER, LYKES BROS. STEAMSHIP CO., INC.; GEORGE F. LOWMAN, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, FARRELL LINES, INC.; AND SPYROS S. SKOURAS, SR., PRESIDENT AND CHIEF EXECUTIVE OFFICER, PRUDENTIAL LINES, INC.

Mr. LOWMAN. That is satifactory, Mr. Chairman.

Senator STEVENS. Mr. Amoss, you are first.

Mr. AMOSS. Mr. Chairman, I have submitted written testimony and I would like to just give a brief summary of our testimony. Lykes Bros. Steamship Company of New Orleans, LA is an American flag-subsidized liner vessel operator engaged in international commerce on five trade routes, mostly from Gulf of Mexico ports and from U.S. West Coast ports and from the Great Lakes.

We own and operate the largest American flag fleet in international liner service, a total of 32 American flag vessels, and the company is also building six container vessels in Japanese yards which will be delivered later this year.

Lykes believes that the build and charter program will be a benefit to U.S. shipbuilders and to the American Merchant Marine and that liner vessel designs incorporating national defense features with viable commercial configurations are an attractive potential that could be developed through this bill.

Lykes has fleet replacement plans which it believes could utilize types of vessels that would qualify for production in American yards under the build and charter program. We have some suggestions for some

changes in the bill as written. Specifically, we suggest that section 1403 prohibiting the eligiblity of vessels constructed under the build and charter program to receive operating differential subsidies should be dropped.

My testimony cites the parallel of vessels allowed to be built in foreign yards and operated under ODS under section 615 of the Merchant Marine Act as well as the administration's currently proposed legislation to permanently amend the Merchant Marine Act to permit foreign-built ships to receive ODS.

Now, we see no difference between this and ships built in American yards and chartered or sold at foreign prices, a they are in economic terms the equivalent of ships built in foreign yards, we believe that if one should be eligible for ODS, the the other should.

We further cite the highly questionable ability of American carriers to compete with foreign competition if ODS is prohibited, and we note that this will affect a level of competitive interest in purchasing or chartering such vessels and may very well inhibit the generation of charter rates available in such transactions that would be needed to help replenish the fund and make it go further.

We also urge the removal of the profit recapture provisions in 1406. This concept was abandoned by the government in the 1970 amendments to the Merchant Marine Act and there were many reasons why this was done.

We would like to point out that if profit recapture is deemed to be a fair and equitable and reasonable concept, then the sharing of losses with the government on a similar basis on the other side of the line should be mandated.

Thank you very much.

[The statement follows:]

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STATEMENT OF W. JAMES AMOSS, JR., CHAIRMAN AND CHIEF EXECUTIVE OFFICER, LYKES BROS. STEAMSHIP CO., INC.

My name is W. James Amoss, Jr. I am chairman and chief executive officer of Lykes Bros. Steamship Co., Inc. ("Lykes") of New Orleans, Louisiana.

Lykes Bros. Steamship Company currently operates 32 American flag ships engaged in the carriage of liner cargoes from ports in the Gulf of Mexico to South America, Africa, Asia, the Mediterranean Sea and North Europe, from the U.S. West Coast to Asia, from the U.S. South Atlantic to the Mediterranean and from Great Lakes ports, during the shipping season, to Mediterranean, Red Sea and Indian Ocean ports. Lykes is the largest operator of American flag ships in our foreign commerce; thus, it is of particular interest to Lykes to present testimony on S. 1885, a bill to provide for the construction in private American shipyards of merchant vessels which would be available for sale or charter to qualified citizens of the United States at world price levels for operation in the foreign commerce of the United States.

As presently proposed S. 1885 has certain prohibitions and limitations that we believe will seriously inhibit the interest of a large segment of the existing liner companies. It should be noted that vessels which have the highest potential for national defense purposes will include liner vessels with certain features such as cargo unloading gear and container, barge carrying and breakbulk cargo capacities. We do not presume that tankers and other specialized vessel types which may be desirable as military auxiliaries would not be considered under this proposal, however, our testimony is confined to the dry cargo liner segment of the maritime industry.

Section 1403 of the proposed bill would prohibit the payment of operating differential subsidy for the operation of vessels provided under the military revolving fund. This prohibition will eliminate the interest of subsidized operators in chartering or purchasing such vessels. The reason for such limitation is not clear since it fails to recognize the need for an American flag operator to operate competitively against his cheaper foreign competition in international commerce. Of perhaps more direct interest to the Navy, the elimination of subsidized operation will result in less competition to buy or charter vessels constructed under this bill reducing possibly to absurd levels the amount of charter hire or the purchase price that might be competitively offered for the operation of such vessels as may be constructed. This, in turn, will detract from the regeneration of the fund in a commercial evergreen manner. It is also noted that section 1402(c) requires the Secretary to charge not less than the cost of a similar vessel constructed in a foreign yard. Congress has in the past permitted the construction of vessels in foreign yards for subsidized service and the administration presently has submitted a bill to again permit foreign built vessels to be operated in subsidized service which is precisely what would result if section 1403 were removed. It is, therefore, urged that section 1403 be eliminated in order to provide a substantial potential market for the sale or charter of those vessels that may be created under the build and charter program.

Section 1406 revives a concept of income recapture which was originally part of the operating differential subsidy system. The concept of recapture was eliminated from the subsidy system in 1970. The reason for this recognition that recapture singled out another competive burden on American carriers in the operation of vessels in international commerce. One imagines that this simple idea has appeal as a modest proposal but in practical terms its threat will be reflected as a detriment to the pricing of sales or charters again affecting the fund as an evergreen piece or maritime legislation. It will require the setting of standards, controls and administration relating to accounting on an annual basis of specific vessels as opposed to company or profit center accounting and represents one more regulatory incursion in the private operation of ships that ought to be eliminated. If it remains then the same spirit that motivated recapture of profit should extend the obligation under section 1406 to the sharing of one-half the net voyage losses in excess of ten per centum per annum.

It is further noted that section 1409 limits the use of vessels built under this bill in either the transpacific or transatlantic dry cargo liner service for a term year period unless these vessels are required to replace existing vessels under an operating differential subsidy contract, and I submit that rates and conditions in these trades which must have promoted this limitation are such that it is unlikely that an ODS operator will have an interest in obtaining a vessel at world market prices only to be forced to operate against foreign competition without the benefit of operating differential subsidy.

These suggested changes, if adopted, will in my opinion strengthen S. 1885 and make it an important basis for revitalizing the private American shipbuilding indus-

try and the private American merchant marine while accomplishing the needed goal of creating new vessels maintained in active commercial service with broad capabilities to serve as naval and military auxiliaries in time of war or national emergency.

Senator STEVENS. Thank you very much.

Mr. Lowman.

Mr. LOWMAN. Mr. Chairman, my name is George F. Lowman. I am the chairman and chief executive officer of Farrell Lines, Inc., an American flag-subsidized international carrier. I am appearing here today to comment on S. 1885, a bill to authorize the establishment of a military auxiliary revolving fund within the Treasury of the United States, amending the Merchant Marine Act of 1986 by adding Title XIV build and charter.

In an appearance before this committee on November 15, 1985, I spoke on behalf of the Council of American Flag Shipping Organization, CASO, and I supported a build and charter program. I stated that the concept, although constructive, offered only an incomplete solution to the problems facing the public and private sectors of the Merchant Marine industry, and I urged that the committee take a broader view of the American Merchant Marine, to include such items as a build and charter foreign program, an expanded Title XI financing program, a U.S. crews with wage differential program, and a deregulation of trade routes program.

Today, I am representing Farrell Lines only and my remarks will be in support of S. 1885. It would be appropriate to give you a brief description of Farrell Lines to point out how a smaller company in the lesser trade routes would be a candidate for this type of build and charter program.

In our trade areas, including the Mediterranean and West Africa, we are not interested in super-size container ships capable of carrying 3,500 to 4,500 TEUs. We are interested in smaller vessels with the capability to carry container break bulk and roll-on/roll-off cargo. The largest container ships are effective on the very heavily trafficked and most sophisticated trade routes.

They require modern container ports with deep drafts and shoreside gear to accommodate them. Many of our ports of call involve Third World countries where the ports are less efficient, thereby requiring our ships to be self-sustaining and capable of loading and discharging with the use of our own gear.

This characteristic, it seems to me, makes our operation more compatible with the needs and desires of the Navy which cannot always find available a sophisticated and modern port able to accommodate the larger container ships.

In most instances, our competition is foreign and employs equipment built in the least expensive shipyards in the world. It is essential, therefore, that Farrell meets that competition head-on so that it is able to provide its commercial shippers with a reliable service at competitive rates.

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Accordingly, it cannot pay more for its ships and other equipment than its competitors pay. Under no circumstances would Farrell be interested in bidding for a Navy ship at a price higher than foreign competitive cost. Such an act would immediately make us noncompetitive. By the same token, we would not expect to receive new construction for less than the price our competition is paying for their ships.

The operation of a modern carrier fleet is not static. It changes from time to time as the needs of shippers change. Any equipment purchased or chartered from the Navy might therefore need to be modified and improved as the conditions in the trade dictate in order that the carrier can continue to remain competitive.

Supplementing the remarks in my previous appearance on record before this committee, I would like to address myself specifically to the following enumerated areas:

SECTION 1402

Section 1402 provides that the Secretary of the Navy may charter vessels constructed under this act " . . . after due advertisement and upon sealed competitive bids." The American Merchant Marine operates in a difficult and highly competitive international industry. Our private companies compete not only against foreign nationals, but in many instances against foreign countries. To be competitive, therefore, the Merchant Marine requires the most modern and efficient vessels it can obtain.

It is unrealistic to think that the Navy can build a complement of ships designed primarily for military purposes but offered to the Merchant Marine for charter and/or purchase, pending their use in military emergencies.

To be competitive and efficient, the ships must be built for the particular trades in which they will operate and cannot be compromised in design or construction without subjecting the carrier to a significant disadvantage.

Therefore, instead of offering ships that have been constructed, the Secretary of the Navy should offer to interested carriers the opportunity to develop plans for ships which will have a primary usefulness to the carrier, but which the Secretary may find adaptable to the Navy with certain modifications and changes.

To the extent such modifications or changes reduce the competitiveness of such ships, the Navy should bear the resultant cost.

A carrier in the Merchant Marine cannot use makeshift equipment, even though brand new, and still be competitive in the difficult international trade in which it is required to operate. Ships that are designed for particular carriers must have the required characteristics to be competitive.

Where the interests of the carrier and the Navy are compatible, and the price that the carrier is obliged to pay is based upon the cost of a comparable ship built in a foreign shipyard, the revolving fund will be fairly compensated without the necessity of competitive bids.

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Such construction should be sold or chartered to the carrier concerned with the understanding that the price basis will be comparable foreign construction cost, less any national defense design features and equipment required by the Navy.

SECTION 1403

Section 1403 states that where a carrier charters or purchases a merchant vessel under the act, it will not be eligible for ODS. Most of the ships owned by present ODS contract carriers were built with construction subsidies.

The purpose of construction subsidies was to provide American carriers with ships comparable in price to foreign competition. A new or replacement ship built pursuant to this act should not be precluded from subsidy, since a purchased or chartered vessel should cost the carrier no more than one built with capital construction funds. ODS relates to wage differentials and should not be affected by the cost of vessel construction.

SECTION 1406

In reading the language of section 1406, it is hard to understand the purpose the legislation is seeking to effect. One cannot determine whether the Secretary of the Navy, by using a competitive bidding process, is attempting to get a return greater than a charter hire based on comparable foreign construction costs, or whether the Secretary is seeking to permit a carrier to realize a bonanza by obtaining the purchase or charter of a ship at less than the value based on comparable foreign costs.

In my view, neither of those alternatives is appropriate. The carrier should pay no more and indeed no less than a value based on comparable foreign construction cost. Accordingly, if the carrier buys or charters such vessels at comparable foreign construction cost and thereafter manages to make a profit on the year's operation, there is no reasonable basis for imposing upon a carrier an obligation to repay a percentage of its profits.

A shipping company's performance varies greatly from year to year. Under favorable international conditions, profits may be high. Under adverse conditions, however, there may be modest profits or even significant losses. I do not suppose the Government is suggesting that in adverse years the Navy would be willing to share the losses.

As I have indicated above, the awarding of ships under a program of this nature should not be based on any consideration other than a comparable foreign construction cost. In such a situation, the carrier would pay the same price that his competition is obliged to pay, and he therefore has the incentive to operate more efficiently and thereby realize a profit.

In previous hearings before members of this Committee, representations were made by American flag carriers and members of CASO that they need many more ships than can be constructed under this Build and Charter Program.

Accordingly, there should be language in this act to provide that those carriers who are not successful in reaching agreements with the Secretary of the Navy for the sale or charter of vessels in a particular year and who are not able to wait for subsequent allocations of money in later years have the right to build or charter foreign.

To fail to provide such an alternative where there is no realistic opportunity to build or charter in the American market would be inequitable and inimical to the best interest of the American carriers needing new equipment for competitive commercial purposes.

SECTION 1408

To the extent section 1408 requires a carrier who builds or charters a vessel under this act to buy insurance in excess of that usually obtained in accordance with reasonable business judgment, such extra cost should be for the account of the Secretary of the Navy.

SECTION 1409

If the language of section 1409 means what it appears to say, only very few carriers will be able to build or charter under this act. Certainly, Farrell Lines could not hold a vessel for 10 years before operating in the trans-Atlantic or trans-Pacific service.

My understanding of the language would lead me to conclude that service from the United States to the Mediterranean area would be a trans-Atlantic service, and therefore ships built under this act would not be eligible for operation until 10 years after construction.

Likewise, ships for use from the United States to West, South or East Africa would be in the trans-Atlantic service. I would suppose that ships from the east and west coast of the United States to Australia and New Zealand would be trans-Atlantic and/or trans-Pacific areas and therefore not eligible except in the event such construction replaces an existing vessel operating with ODS or replaces a vessel over 25 years of age or commercially obsolete.

I do not fully understand what this section is designed to accomplish, but if I read it correctly Farrell would not be able to participate in the program.

In reply to the specific questions raised in the Chairman's letter dated February 4, 1986:

MarAd would be the appropriate agency with which the carriers should deal under the proposed legislation. The Maritime Administration is composed of private citizens with varied and many faceted areas of training and experience who are more likely to understand the competitive nature of the private shipping business.

The Navy is a command structure that has a specific purpose and permits little deviation or modification of the rules under which it is required to operate. It sometimes gets overburdened with its authority and has problems operating in the private sector.

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For most carriers in the American Merchant Marine, the problem of overtonnage is subordinate to the necessity of obtaining modern, competitive equipment. Under the Shipping Act of 1936 and its amendments, all American ships constructed prior to the last 3 or 4 years have been powered by steam turbines to meet the defense requirements of the U.S. Navy. Most of those ships are still relatively young as to age but old as to design and efficiency.

Most carriers, therefore, are seeking to replace their expensive steam-turbined operations with slow speed diesels which consume less fuel at a lower cost and require fewer in crew to operate and maintain them.

Therefore, despite overtonnage in the industry a Build and Charter Program to provide modern, efficient, effective equipment is desirable. If the Navy insists that new construction under this Act should include steam turbines, then appropriate financial allowances should be provided to compensate the carrier for any additional costs he incurs which would make him noncompetitive.

I have dealt with the economic feasibility of chartering in the light of these specific limitations imposed by the Act in my remarks above.

Thank you very much. I will be pleased to answer questions if I am able to.

Senator STEVENS. Thank you. Mr. Skouras.

Mr. SKOURAS. Senator Stevens, I am President and chief executive officer of Prudential Lines, Inc., one of the remaining seven U.S. flag liner companies. I will give a shorter version of my submission to you.

Prudential Lines appreciates the opportunity to testify before you today at this Build and Charter Program hearing on S. 1885, a significant legislative proposal that could substantially help the current state of the United States Merchant Marine. We are encouraged by this subcommittee's continued support of and interest in the U.S. Merchant Marine and the U.S. flag liner industry.

As you will recall, I testified before this subcommittee on November 15, 1985 in connection with S. 1832 and S. 1833. My testimony on that day supported in concept the legislation then proposed with certain suggested amendments.

My comments today will focus primarily on the three concerns raised in Senator Stevens' letter of February 4, 1986 inviting me to testify before you regarding S. 1885.

One, the appropriate role of MarAd in the consultative process: Prudential believes in general that the Maritime Administration in the past has contributed greatly by overseeing legislative programs that are wisely drafted. Prudential endorses a provision that would give MarAd a role in the consultative process, if the Maritime Administrator, Mr. John Gaughan, personally reviews the implementation of such a program.

The appropriate role of MarAd is to guarantee priority to the small liner companies. Prudential could not endorse a Build and Charter Program which did not specify that each of the three small liner companies would be provided with new vessels on a priority basis over the larger liner companies. Vessel selection should be determined on the

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basis of the needs of each of the small liner companies consistent with the national interest rather than on a purely competitive basis.

Two, the existence of overtonnage in categories of vessels proposed to be constructed: The Navy has stated they are in great need of certain vessels such as small tankers, heavy-lift vessels and roll-on/roll-off vessels for their present requirements today and their future needs in potential emergencies. Since the building of these vessels is not economically justified in the commercial marketplace, the Navy should proffer back-to-back long-term charters to the small liner companies on a sole source charter at reasonable profit, determined by MarAd.

If the Navy's vessel selection is such that the Navy cannot justify long-term charters at a reasonable profit as determined by MarAd for each of the three small liner companies, then the Secretary of the Navy should not be permitted to select that vessel because there would not have been an adequate demonstration for the need for that vessel.

Since the vessel will have a demonstrated commercial and military need, there is no reason to resist having the vessels chartered on a back-to-back basis by each of the three small liner companies.

Three, the economic feasibility of chartering in light of the specific limitations on markets, subsidy and charter fees imposed by S. 1885: Prudential believes that it is appropriate for the Navy to be required to demonstrate that its need for vessels is supported by the Navy's willingness to charter the vessels for use by the U.S. Merchant Marine for long-term charters. Specifically, the Navy should be required to charter on a first priority basis to each of the small liner companies such vessels from the Navy on a sole source basis. Subsequently, each of the three small liner companies should receive long-term charters on such vessels from the Navy at a reasonable profit, determined by MarAd.

Furthermore, Prudential opposes the Secretary's arbitrary discretion to reject a bid based on the charterer's financial resources and credit standing. This would be an unreasonable discretion against the small liner companies which could operate to the detriment of the U.S. Merchant Marine.

Four, the need to strengthen the U.S. Merchant Marine to deregulate and to provide in the national interest for a world competitive Merchant Marine: Senator Stevens and Senator Inouye, in previous meetings with the representatives of the U.S. Merchant Marine, have properly indicated their concern for the alarming rate at which the U.S. Merchant Marine has been declining in terms of its number of vessels and financial strength. As the Senators well know, there are active discussion at the present time which hopefully will lead to legislative proposals to strengthen the U.S. Merchant Marine.

While I do not wish to prejudge any proposed ultimate legislative program which Prudential may or may not support, certain facts are clear. Operating Differential Subsidies presently projected will not satisfy the goals of the companies wishing to enter the ODS program.

The three small liner companies will undoubtedly be asked to not resist immediate or virtually immediate subsidized competition on their trade routes. In Prudential's view, each of the three small liner com-

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panies, will require reasonable financial support to have the borrowing power and capital to build new vessels with which they can compete and participate in any new deregulated environment.

The original concept for the Build and Charter Program as with all legislative proposals, has undergone evolution. We now see the Build and Charter legislation proposed by the Senator in a form different than was originally proposed. Nevertheless, the original concept which the Senator had for using the Build and Charter Program as a potential component for the benefit of the entire Merchant Marine is a valid concept which we would urge the Senator to continue to press.

If the Build and Charter Program is used as it was originally intended to be used, in part to benefit the U.S. shipyards, in part to benefit the U.S. Navy, and in part to benefit the U.S. Merchant Marine, including the small liner companies, the Build and Charter Program will be a worthy one which Prudential could support.

Thank you.

Senator STEVENS. Thank you very much.

I know from the number of meetings that we have had together, gentlemen, that you have spent a lot of time on the whole subject of trying to maintain the competitiveness of the industry. I believe that we are just going to have to keep working until we find some solutions, not only in this area but in many other areas.

Let me say that I certainly understand the comments you have made about specific provisions, and we will take those into account.

There is no question about the profit section. The profit recapture section has to be reviewed, and I think that issue brought up by you in the first instance, Mr. Amoss. I think that the Farrell comments go to the same point. I understand and do not necessarily disagree with the specific comments on a number of the sections. I think that we will have to have some further conversation concerning at least one of those sections, Mr. Lowman. We will have that.

You are absolutely right that the carriers should pay no more and no less than the value based upon comparable foreign construction cost, and that is the basic tenant of this bill.

Mr. Skouras, we also agree with you about your priority for small companies. I think that is built in with many other aspects of Federal law, and we certainly would not countenance any action that would, in the name of saving an industry, destroy competition within it. You may rest assured that we will take heed to your comments in that regard.

I had hoped that by the time we got to this hearing we might have a little different situation with regard to some other pieces of this puzzle so that they would fit together. It is not apparent to me yet, but I think that we are going to have to just follow your last comment and keep working to try to find a comprehensive solution to all of these problems, including the one that we know is out there today on a very current basis regarding the future of SWAP.

I have no particular questions because I do not disagree with your comments.

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Senator Long, do you have any comments?

Senator LONG. I just got here, Mr. Chairman, but I am glad you are holding these hearings. I had a chance to visit Mr. Amoss about this matter prior to this time. I hope very much that we are able to do something effective to help the Merchant Marine because it is sorely needed. I appreciate your doing this.

Senator STEVENS. Thank you. Those are constructive suggestions. We appreciate having them.

Now, Mr. Finnerty and Mr. Erik Johnsen.

STATEMENTS OF PETER J. FINNERTY, VICE PRESIDENT, PUBLIC AFFAIRS, SEA-LAND CORPORATION; AND ERIK F. JOHNSEN, PRESIDENT, CENTRAL GULF LINES, INC., ACCOMPANIED BY EDWARD L. MERRIGAN, COUNSEL

Mr. FINNERTY. Thank you, Senator. I will, with your permission, submit our full statement for the record and just summarize my comments.

Sea-Land is pleased to again appear in support of the concept of Build and Charter in general and the approach taken in S. 1885 in particular, with certain reservations. The bill would, however, be more beneficial to the U.S. shipyard industry and the U S Merchant Marine industry by including the following modifications.

Vessels built under the program should be excluded from all domestic trades covered by the Jones Act, including the noncontiguous trades. In this regard, the Jones Act study required by section 1410 should be undertaken by Congress rather than MarAd in our opinion.

Since the new vessels are ineligible for ODS under the bill, for each such vessel acquired a subsidized liner operator's ODS contract should be amended by making proportionate reductions on a vessel productivity basis in the number of subsidized sailings and vessels.

All liner operators, whether or not they have an ODS contract, should be able to charter or purchase the vessel and use it as a replacement vessel within the ten-ye r period after construction but operate the Government-built ship without the additional Government expenditure for ODS.

The bill should specify the standard to be used by the Secretary in estimating the foreign construction costs of vessels. The Secretary should make this cost comparison by referring to foreign shipbuilding centers, one, which have the ability and experience to construct the proposed vessel and, two, which a prudent U.S. purchaser would consider to be a reasonable risk.

The bill should establish a minimum charter price which relates to the usual commercial criteria to insure the Government a fair return on its investment.

The responsibility criteria applied to vessel charterers in section 1405 should be extended to apply to vessel purchasers as well.

The bill should contain criteria to be used by the Secretary in evaluating proposals to construct different types of vessels. This will insure that the vessels are militarily useful and commercially competitive.

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Sea-Land also assumes that S. 1885 would not allow RoRos acquired for the Ready Reserve Fleet and retrofitted at Government expense to compete against private sector commercial carriers.

Thank you very much.

[The statement follows:]

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STATEMENT OF PETER J. FINNERTY, VICE PRESIDENT, PUBLIC AFFAIRS, SEA-LAND CORP.

The following comments are submitted by Sea-Land Corporation, parent of the liner carrier Sea-Land Service, Inc., regarding S. 1885, the build and charter bill introduced by Senator Stevens on November 23, 1985.

In our November 15, 1985 testimony to the Subcommittee on Merchant Marine of the Senate Committee on Commerce, Science, and Transportation on S. 1832 and S. 1833, Sea-Land stated its support for the concept of build and charter in general, and the approach taken in S. 1833 in particular. Sea-Land similarly supports the approach of S. 1885, with certain reservations. In our earlier testimony we had proposed several revisions to S. 1833, and were, therefore, very encouraged to see many of these points addressed in S. 1885. In addition, Sea-Land believes that the modifications to the build and charter program set forth in S. 1885 which are aimed at better protecting the Government's investment in the vessels built under this program make this a stronger bill.

In these comments we will not discuss each provision of S. 1885. Rather, we will address a few proposed amendments to S. 1885 which Sea-Land would ask the Committee to consider. We are also attaching to these comments a redraft of S. 1885 with the revisions superimposed. With these amendments, Sea-Land believes that S. 1885 will be beneficial to the United States shipyard industry and the United States merchant marine industry.

Prior to discussing these revisions, however, Sea-Land would like to express its support for the fact that, unlike an earlier build and charter proposal, S. 1885 would be available to all segments of the shipping industry, bulk carriers and liners alike. Sea-Land believes that it is imperative that any build and charter program which is enacted be for the benefit of the entire merchant marine industry.

As was the case with S. 1833, Section 1403 of S. 1885 provides that charterers or purchasers of vessels constructed pursuant to this program cannot receive ODS for the operation of such vessels. Sea-Land strongly endorses this provision as well as the requirement of Section 1409 that liner operators may not use these vessels for ten years after their construction, unless the Secretary finds they are required as replacement vessels. Sea-Land would further propose that the ability to charter or purchase such vessels and use them as replacement vessels within the ten year period be available to all liner operators, whether or not they have an ODS contract. Since these vessels will be ineligible for ODS, however, for each such vessel acquired, a subsidized liner operator's ODS contract should be amended by making proportionate reductions on a vessel productivity basis in the number of subsidized sailings and vessels. As we indicated in our November 15, 1985 testimony, this amendment to the bill would be consistent with the purpose of the 1970 Amendments to the Merchant Marine Act, 1936 of reducing liner operators' reliance on subsidy, and President Reagan's statement of October 15, 1985.

Section 1402(c) provides that the purchase price of the vessels constructed pursuant to this program cannot be less than what would have been the cost of constructing the vessel outside the United States. This bill, like S. 1833, does not take into account the fact that foreign construction costs differ substantially from country to country. Sea-Land believes that the language we proposed for S. 1833, which would establish a standard to be used to make the requisite cost comparison, should also be included in this bill. That is, the Secretary should be required to determine the estimated foreign construction cost by reference to foreign shipbuilding centers which: (1) have the ability and experience to construct the proposed vessel, (2) could reasonably assure delivery in accordance with contractual requirements, and (3) are located in countries where a prudent U.S. purchaser would have its vessels constructed.

Section 1405 of S. 1885 requires the Secretary to award charters to the highest offeror, and in awarding such charters the Secretary must consider certain responsibility criteria. These criteria are, the charterer's financial resources and credit standing, practical experience in the operation of vessels, and any other factors a prudent businessman would consider. Further, the bill permits the Secretary to reject a bid if the charter hire is considered too low to adequately replenish the Fund.

Sea-Land believes that these provisions, which were not included in S. 1833, are very positive elements of this legislation and will serve to more adequately protect the Government's interest. We would, however, propose two additional provisions. First, the bill should establish a minimum charter price, relating to the usual commercial critieria, which insures the Government a fair return on its investment. Second, the responsibility criteria should be extended to apply to vessel purchasers as well. The application of these criteria to both classes of program participants

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would promote the sale and charter of these vessels to entities with the experience and capability to assure proper commercial operation of the vessels, and prevent speculation.

In connection with S. 1833, Sea-Land had proposed standards to be used by the Secretary in evaluating the different proposals to construct different types of vessels. We believe that these standards should also be included in S. 1885 so that the vessels constructed will not only be militarily useful, but will also be a positive commercial venture. These standards should encompass the following factors: (1) the military utility of the vessels, (2) the commercial competitiveness of the vessel, (3) the need for the vessel in the trade in which it will be deployed, and (4) the potential for creating overtonnaging in the proposed trade and with respect to vessels of the type proposed.

Section 1409(b) prohibits the use of the vessels constructed under this program in the coastwise and intercoastal trades. Sea-Land believes that this prohibition should be expanded to encompass all of the domestic trades covered by the Jones Act, including the noncontiguous trades. In additon, Section 1409(b) should be amended by deleting the authority of the Secretary of Defense to direct a waiver of the Jones Act prohibition if he considers it to be in the interest of national defense. There should be no exception to the Jones Act trade prohibition short of a Presidential declaration of national emergency. As we noted in our November 15, 1985 testimony, operators in the domestic trades have relied upon the Government's commitment that vessels constructed with its shipbuilding assistance would not be allowed to operate in the Jones Act trade. Domestic operators would be placed at a severe competitive disadvantage if such new Government-funded vessels were permitted to enter the Jones Act trade.

Sea-Land would also propose deleting Section 1410 which directs the Maritime Administrator to conduct a study of the workings of the Jones Act. Since such a study would undoubtedly serve as the basis for future legislative proposals, Sea-Land believes that the study should be undertaken by Congress itself.

Mr. Chairman, I believe that in the Continuing Resolution $228 million was appropriated for the acquisition of vessels for the Ready Reserve Force, and it was anticipated that such vessels might be retrofitted from the $228 million appropriated in the Continuing Resolution or the $850 million covered by this Bill which was also appropriated in the Continuing Resolution. Sea-Land supports the promotion of vessel construction and repair work in United States yards. We would, however, object to allowing retrofitted RoRo vessels to compete against private sector commercial carriers. We assume that restrictions on the commercial operation of any such retrofitted vessels would be applied by S. 1885 as well as covered by this Bill.

Sea-Land has appreciated the opportunity to submit its views on this important piece of legislation, and if the Committee wishes, we would be pleased to provide any additional assistance or information which is required.

Senator STEVENS. Thank you very much. Mr. Johnsen.

Mr. JOHNSEN. Thank you, Mr. Chairman, and thank you for the invitation to appear before your Committee today. I have submitted my statement for the record and will simply summarize the contents of that statement.

Central Gulf Lines supports the enactment of S. 1885 but only with an amendment which provides for removal of the three-year statutory prohibition against the transport of Government financed cargoes in U.S. flag vessels constructed abroad.

Without such an amendment, S. 1885 would enable the Navy to construct the type of special purchase merchant vessels it needs for national defense purposes, and it would provide a badly needed economic infusion for the domestic shipyards.

It will not, however, enable the U.S. merchant fleet to acquire the number and type of new modern vessels it desperately requires to compete against aggressive foreign merchant fleets. Existing economic conditions, including extremely high construction costs, construction delays

and the recent demise of the Federal Construction Subsidy Program simply make it impossible for U.S. flag operators to finance and build the ships they desperately need in the U.S. shipyards.

Simultaneously, the Federal cargo preference laws effectively preclude U.S. operators from constructing any new U.S. flag vessels in foreign shipyards. Under those Federal statutes, a new U.S. flag vessel built in a foreign yard is prohibited from carrying Government-financed cargoes for three years.

Construction of the U.S. flag vessels in foreign yards, financed entirely with private capital will have no adverse effect on the Federal budget, and it could lead to substantial savings in the cost of transporting Government-financed cargoes.

U.S. shipbuilders have recently indicated that they realize the economic necessity for relaxation of the three-yer prohibition against transportation of Government cargoes in newly-constructed U.S. flag vessels built abroad, so clearly now is the time to provide for the construction without penalty of at least a specific number of such vessels in foreign yards.

Thank you very much.

[The statement follows:]

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STATEMENT OF ERIK F. JOHNSEN, PRESIDENT, CENTERAL GULF LINES, INC.

Mr. Chairman, I am pleased to appear before the Committee today, in response to your invitation of February 4, to present my views on S. 1885, a bill introduced late last year to provide for the establishment of a build and charter program.

From the very outset, I want to commend you, Mr. Chairman, as well as the other members of this committee interested in this legislation, for realizing that the U.S. flag merchant fleet is in serious decline, and that a compelling need exists for the construction of new, modern merchant vessels capable of serving as naval and military auxiliaries in time of war or national emergency. Clearly, if the U.S. merchant marine is to survive and again compete effectively—and if our nation is to be prepared for whatever emergencies lie ahead—both the private sector and the military must be permitted to acquire new, up-to-date vessels at prices that are reasonable and affordable.

S. 1885 is thus a sound, salutary step in the right direction because—

(1) it will enable the Navy to construct the type of special-purpose merchant vessels it requires for national defense purposes;

(2) it will provide a badly-needed economic infusion for U.S. shipyards withdrawn from the construction of the kind of merchant vessels our countrty needs; and

(3) to the extent some of the vessels the Navy builds may be competitively utilized by the private sector U.S. merchant fleet, the bill authorizes the Navy to charter and/or sell those to U.S. citizens at reasonable rates and prices.

However, the committee must surely realize that while S. 1885, in its present form, will assist the Navy and benefit U.S. shipyards it will do nothing significant to enable the private U.S. merchant fleet to acquire the number and type of new, modern vessels it needs to continue to operate and compete more vigorously against the merchant fleets of other maritime nations throughout the world. Existing economic conditions, including extremely high construction costs, construction delays and the recent demise of the federal construction subsidy program, simply make it impossible for U.S. flag operators to finance and build the ships they desperately need in U.S. shipyards. Simultaneously, the federal cargo preference laws effectively preclude U.S. operators from constructing any new U.S. flag ships in foreign shipyards. Under those federal statutes a new U.S. flag vessel built in a foreign yard is prohibited from carrying Government-financed cargoes for three (3) years.

In sum and substance, therefore, if S. 1885 is enacted in its present form some specially-constructed Navy vessels might ultimately trickle down to the U.S. merchant marine, but the U.S. flag operators will remain powerless to build the number and type of new, privately-owned vessels they desperately need in U.S. shipyards, and they will still be effectively precluded by the cargo preference laws' 3-year waiting period from building abroad.

Consequently, I support the enactment of S. 1885, but only if it is amended to provide for the removal of the 3-year statutory prohibition which presently precludes the transportation of preference cargoes in new U.S flag vessels constructed abroad. This amendment is essential to assure that both the Navy and the private U.S. merchant fleet are able, without further delay, to obtain the number and variety of vessels they need. Construction of U.S flag vessels in foreign shipyards will, of course, be financed entirely with private capital, so adoption of the proposed amendment will not require the use of any federal funds and there will be no adverse effect on the federal budget.

Moreover, in recent testimony and informal statements, representatives of the U.S. shipyards, which obviously will benefit significantly from enactment of S. 1885, have indicated the domestic yards now realize, in light of compelling adverse conditions throughout the maritime industry, that some liberalization of the 3-year cargo preference prohibition applicable to new, foreign-built U.S. flag ships is warranted.

I believe U.S. flag operators also generally agree, so I suggest the adoption of an amendment which would make foreign-built ships eligible for transportation of preference cargoes immediately upon documentation under the U.S. flag. For the present at least, the number of eligible vessels might be specifically restricted, to say 50; and in order to promote the early creation of a modern, up-to-date U.S. fleet, I submit eligibility should be limited to newly-constructed vessels only—certainly to vessels that are not more than 3 years old.

Finally, as Chairman Stevens recognized last year when he introduced S. 1832 and 1833 on November 5, I submit that whatever programs are finally authorized under S. 1885, must be fashioned to prevent the granting of unfair competitive advantages to one or more U.S. flag operators over U.S. flag competitors. Thus, S. 1885 should carefully prescribe that U.S. flag operators who charter or purchase Build-Charter program vessels, or who acquire eligible foreign-built U.S. flag vessels

under the legislation, shall not be eligible to receive Operating Differential Subsidy payments for the operation of such vessels, unless of course S. 1885 (or other legislation) provides for Operating Differential Subsidy contracts and payments to competing U.S. flag operators on an essentially equal basis.

When our Executive Vice President, Mr. Grehan, testified before this Committee last year, he urged the competing segments of the U.S. merchant fleet to reach a reasonable accommodation in these areas, and I am happy to report that seemingly much progress has since been made in this regard, at least to the extent of drafting the type of legislation necessary to provide "a level federal playing field" for the competing industry components. Much remains to be considered but certainly S. 1885 should be modified to provide that the Build-Charter program, and foreign construction amendment I propose, will be designed to operate fairly and evenly among the surviving, competing segments of the U.S. merchant marine.

CONCLUSION

On behalf of Central Gulf Lines, Inc., therefore, I support the enactment of S. 1885 with the vitally important amendments I have described. With such amendments, the legislation would clearly be in the national interest and it would be of great benefit to our national defense, to the nation's shipyards and to the U.S. merchant marine.

Senator STEVENS. Thank you. You have raised an interesting question, Mr. Finnerty because the staff has called to my attention the Journal of Commerce article of March 20 dealing with the proposal for an anti-recession cartel of Japanese shipbuilders. It certainly would be necessary, I should think, to have the kind of standards that you mentioned with regard to the manner the Secretary would use in estimating foreign construction costs.

Otherwise we might find ourselves suddenly supporting a new overseas cartel. That could lead to some real difficulties.

You both have questioned the ODS issue and the 3-year prohibition on the carriage of the preference cargoes. Those are very controversial issues I am sure you realize. Within your industry itself, have there been any later meetings that we are not familiar with concerning those two issues? The first is the problem of ODS and the second is the question of the 3-year prohibition.

Mr. JOHNSEN. As far as I know, Senator Stevens, we have had meetings on the various concepts. You mentioned a moment ago the question of SWAP. We made what I consider to be a great deal of progress in that area. I think we have some areas that we trust that we can attack and also settle. I think if we can resolve those problems, some of these specific problems would be eliminated because that would be all encompassing in that agreement.

So I think we can say yes, we have had meetings on that, but until we get what would be a level playing field, I think we still have a problem with where the unsubsidized line has great difficulty competing without getting their participation in preference cargoes. They have great difficulty in renewing their fleets if they do not have the ability to get ships at competitive prices.

Which comes first, the chicken or the egg?

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Senator STEVENS. Did you have a comment, Mr. Finnerty?

Mr. FINNERTY. I would just echo Mr. Johnsen's remarks, Senator. There have been meetings. We have continued, since our discussions at the hearing which you conducted late last year, to explore potential solutions to the difficulties.

You have very accurately put your finger on what is fundamental in equality in terms of the structure of the policies of the Government today which manifests itself in statements that each of the different segments of the industry have to then present when we comment on proposed legislation such as the bill before us today.

Because of the different positions that the Government's policies cause for each segment of the industry, their reactions have to be different when we offer our comments on the proposals.

We have explored those solutions, and we continue to try and resolve the differences.

Senator Stevens: Well, we stand ready to continue to work with your industry to try to work out these problems. I know that we are not going to raise this subject here today, but we do have a review going on of the recent SWAP meetings, which I hope to be able to catch up with.

I have got to go back to my state this weekend, but I hope we can get back to it by Tuesday to see what the status of SWAP is.

I think Senator Inouye and I are full of admiration for those of you who take so much time to try and see if there is any way to reach a consensus that would have Administration support, and we are just going to have to keep trying until we find it.

There are problems here that just have to be resolved, and if you can resolve them without our help we would welcome that. But if you need our help, we are available.

Senator Long, do you have any questions?

Senator Long: No questions. I am just glad to see Mr. Johnsen here.

Senator Stevens: We thank you very much. I understand your positions. They are like some other positions. They are not new, but we are pleased to have them stated again.

Mr. JOHNSON: Thank you very much.

Mr. FINNERTY. Thank you, Senator.

Senator STEVENS. Next up is Mr. Drozak, president of the Seafarer International Union.

And for the information of anybody that is concerned with it, Senator Long asked to find out and we did find out that the House rejected Nicaguan aid by a vote of 210 to 222.

STATEMENT OF FRANK DROZAK, PRESIDENT, SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA, AFL-CIO

Mr. DROZAK. Mr. Chairman, I would like to submit my statement for the record because of time, and instead just make a few comments and answer any questions that you or Senator Long may have.

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Mr. Chairman, we support this concept fully and we think it is the right approach. We also think, from listening to the many comments and statements before this Committee and also before the House Merchant Marine Committee and also the House Armed Services Committee, that something has to be done.

We are almost at the point of no return. The shipping companies have a problem and so do the ship builders. I have proposed in my statement that, in order to compromise both issues and help create some jobs for the seagoing membership, the build and charter proposal be coupled with foreign building, and in coupling it with foreign building allow those ships immediate access to Government impelled cargo.

Their argument in many of our discussions, the type of ships do not fit the type of trade. Most of these companies use feeder service ships overseas. The Navy has said they need certain ro ro ships, they could use smaller container ships, and they need tankers.

It would seem to me that this would be the area that we should begin to deal with, allowing three ships built foreign for every one of these ships built under this program built in the United States to either be put in use as feeder services in foreign commerce or in military service, where we are short of these type of small ships for military use.

It behooves me, Mr. Chairman, to sit here and see that Russia has 2,700 ships. They have got a 5-year plan to build 500 more ships. They have just allocated those bids to the communist bloc countries for building, and even Cuba is getting a few of China's ships to build.

Now, we are sitting here with an industry with only 401 ships, a shipyard base that is declining. In both industries we are losing experienced shipbuilders and qualified people that sail the ships.

I testified before the House this morning on the auto carriers. We have today as we sit here some 16,000 jobs in the deep sea maritime industry. We have 35,000 professional seamen to man those jobs. I do not know where we would find the qualified manpower to fill all the ready reserve vessels if an emergency developed. I listened to what Assistant Secretary Pyatt said before the House Armed Services Committee, where he said we could use reservists to crew ships that would have to be broken out from the Ready Reserve Fleet.

My question to him is, and I ask this committee to also consider: Who would man the battleships and the destroyers and submarines, et cetera, if we were in conflict? I am talking about now those ships that have been built and bought and put into the Ready Reserve Fleet.

So I think it is time that this Committee, this Administration, makes up its mind: What are we going to do with this maritime industry? We have sat here and heard this administration oppose everything. Do they have a program or do they have a plan or a future for us? And is the merchant marine and the shipbuilding and mobility base in this country important enough for national security to do something about it?

I do not think the question of money should be there. If we believe it is important, then we should do something about it.

I would certainly work with this Committee, as I always have. There are disagreements, and I do not think you will ever get everybody to agree. Somewhere along the line however, we are not going to have the opportunity to even discuss agreeing, because nothing is going to be there. Every one of the ship owners today are in bad trouble, if they will admit it. They are not going to make it unless positive action is taken in the near future.

You talked about the question of SWAP, and while it is not the subject of today's hearing, still I think it has to be dealt with and dealt with immediately. Otherwise we are going to lose several of these companies, if not all of the remaining seven that we have left.

And so I think that concludes my comments here today since we are running out of time. Sadly, I believe, we are going to have a funeral one of these days and it will be over the American merchant marine.

Thank you.

[The statement follows:]

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STATEMENT OF FRANK DROZAK, PRESIDENT, SEAFARERS INTERNATIONAL UNION

Mr. Chairman, on behalf of the Seafarers International Union (SIU), I would like to express my pleasure in appearing before the Subcommittee once again on the subject of build and charter. The continued interest in establishing a federal build and charter vessel construction program has renewed my optimism that the U.S. maritime industry will yet be revitalized. I sense that after many long years, a consensus may finally be emerging which will permit the enactment of a positive and broad-based promotional initiative that will boost the health of the American shipbuilding industry, and expand employment opportunities for U.S. shipyard workers and seafaring personnel.

Already, a major hurdle towards this goal has been overcome. Thanks to the able and dedicated efforts of the Subcommittee's Chairman and its members, initial funding for a vessel build and charter program was last year legislated into law. Now, proper authorizing legislation to implement the program itself must be enacted. It is important that this be done quickly. However, it must not be done recklessly. The Subcommittee has an opportunity to fashion a program that will provide the broadest benefit to the entire industry, including both domestic shipbuilders and vessel operators. It is my hope that the Subcommittee, the Congress, and the entire U.S. maritime industry will work together for the adoption of a balanced bill, so that a beneficial and enduring program can be forged. I personally assure you that the SIU remains committed to this process, and will work diligently and faithfully for the enactment of a favorable program.

Mr. Chairman, the specific build and charter proposal before the Subcommittee today is S. 1885, a bill introduced in response to an initial hearing held by the Subcommittee last November. As currently written, the legislation would be highly beneficial in severe important respects:

(1) It would provide business to commercial U.S. shipyards which, because of extensive foreign government subsidization and cut-rate labor available in overseas shipyards, have been few new buildings since 1980. Build and charter would provide critical commercial business opportunities to preserve America's essential shipbuilding mobilization base from further decline;

(2) It would generate the construction of new U.S.-flag tonnage. This tonnage would be constructed with defense features built into the vessels, and could be tailored to fit into the Nation's foreign trades. The addition of these vessels to the active fleet would heighten America's security by increasing the number of militarily-useful vessels that are ready at a moment's notice to serve as a defense auxiliary;

(3) The cost to the government of implementing a build and charter program would be small in comparison to the economic and national seucrity benefits it would provide. While the federal government would incur some initial outlays to implement the program, these costs in time would be returned to the Treasury from the sale or charter of the ships, the corporate tax revenues of those companies that build and operate the ships, as well as the payroll taxes of shipyard workers and shipboard personnel; and

(4) The program would provide new employment opportunities for American shipyard workers and the pool of seafaring personnel who are needed to man the vessels required to satisfy our Nation's strategic sealift requirements.

We believe that S. 1885 is a major step in the right direction in strengthening both America's maritime industry and national security. However, we feel that the present proposal still leaves a number of questions unanswered and several issues unaddressed. While it does broaden the scope of the program to facilitate the construction of a much wider range of merchant vessels and includes a requirement that the Administrator of MarAd provide consultation to the program, provisos that would significantly enhance the program's commercial considerations, it lacks elements which could further benefit the overall industry and strengthen the competitiveness of the U.S. fleet versus foreign operators.

To date, the build and charter bills which have been proposed are primarily intended to assist U.S. shipyards. While they would also provide a source of new vessels for the U.S. fleet, this capacity is limited by federal budget constraints and the program's emphasis toward vessels with a high degree of direct military utility. It is not likely that the vessels the Defense Department would be seeking under build and charter would be the type needed for the commercial trades. If the program were to be expanded, however, to incorporate additional elements which enhance the commercial competitiveness of the U.S. fleet while simultaneously generating work for U.S. shipyards, it could be built into a broader and more effective measure.

A more effective policy, which would benefit both shipyards and ship operators, would be to combine build and charter with authroity to build abroad. While build

and charter would provide business to U.S. shipyards to preserve our crucial domestic shipbuilding mobilization base, foreign build would allow American operators to obtain needed tonnage on equal terms as foreign operators. Foreign build would not only facilitate the construction of commercial vessels which would not likely be built under build and charter, it would promote the acquisition of vessels powered by slow-speed diesel engines, a technology which increases operating efficiency and reduces fuel costs, and enhance the responsiveness and competitiveness of U.S. operators through quicker delivery of vessels.

Foreign built authority could also benefit U.S. shipyards thorough a stipulation that operators who build foreign must also construct vessels in U.S. yards. I would suggest, Mr. Chairman, that build-foreign authority be based on a three-for-one formula, whereby an operator may build three vessels abroad for everyone build domestically. This requirement would compliment the intent of the build and chartrer program by providing a steady amount of supplemental business for U.S. yards, business beyond that provided by build and charter alone. Variations of this concept have been considered in the past, and I believe that another review of this proposal may be in order.

The SIU firmly believes that expanding S. 1885 to incorporate foreign build would act to more throughly revitalize the U.S. merchant marine better than any other proposal short of guaranteeing additional cargo. Business for domestic shipyards would be generated, and U.S. operators would be provided an efficient and effective means of modernizing the fleet. I encourage the Subcommittee to fully consider this proposal as a viable option to assisting these critical American industries; it is imperative that a major effort to boost the U.S. merchant marine be implemented before the industry declines still further. A build and charter program such as provided in S. 1885, coupled with the proposal I have described, would initiate such a revitalization.

Thank you.

Senator STEVENS. Thank you. And again, I appreciate your willingness to join in on these discussions when they have been held and to try to find some answers to the problems.

I know that the question that you raised about the availability of manpower in an emergency has been addressed at length in the House hearings, and I know you were involved in those.

We are very interested in this new development. What is this new agreement that we hear which involves the Japanese car carriers and U.S. seamen? Are you involved in that?

Mr. DROZAK. We have one company who has signed a contract just this week with Toyota, I believe, for one ship. We worked out an agreement with the shipowner that is competitive with the Japanese as far as crew cost is concerned.

I understand the ship will be built in Japan. That was one of the conditions, I think. I am not speaking for the company but I believe that we can carry the automobiles as cheap as they can.

But Senator, what has happened since then is that a Japanese publication has come out saying that the wage increases that would be given to the All-Japanese Seamen's Union, shipbuilders, et cetera, not be allocated because of the narrowing of costs between the Americans and the Japanese.

And so it raises a concern for me. We are being competitive with them for this contract. However, they have already taken the initiative to decrease the cost of operations so that we cannot be competitive. I do not know the answer to it.

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The real answer, I think, are the bills that are over in the House, either bilateral shipping agreements or require them to carry a minimum percentage of auto exports on U.S.-flag vessels. If we can carry it as cheap as they can or within the same range, then we should be entitled to 50 percent. Why should the market be closed for us and open for them?

Senator STEVENS. It is apparent we are witnessing a cartel system that is not available under our laws. That is another thing that comes out of this *Journal of Commerce* article today. Did you see that, Senator?

The article indicates that competitiveness is very difficult to maintain. It raises some nice questions, as was just pointed out by the previous witnesses, about the standards used by the Secretary of the Navy to determine what the costs of foreign construction would be.

But we appreciate your help.

Senator Long, do you have any questions?

Senator LONG. You mentioned that you had, as you said, the maritime industry has 16,000 jobs, I think you said. Are those 16,000 jobs now jobs that your members, that the seafarers, for example, could hold?

Mr. DROZAK. That is the total by the Maritime Administration's figures that have just come out this past week.

Senator LONG. And I take it that under previous policies where we were maintaining more of our ships at sea, there might have been jobs for most of your 35,000 seafarers at one time; is that correct or not?

Mr. DROZAK. It would have been 35,000 seafaring jobs and 70,000 seafarers, is what it would be. You see, Senator, too, while the tonnage has not dropped that much, maybe it has increased some, but the manning on board these ships have dropped from 44 men on a ship down to 21 now, and probably will go down to 18.

I hope the shipowners are not listening, but I predict it will be down to 18 men on board these ships in the next few years. So you do not have any excess. There is no fat out there at all.

Senator LONG. Now, those ships, I take it you have larger ships and they are with smaller crews, I take it. Could you give us some idea as to what is the size of the average ship compared to what it was back, oh, 20 years ago?

Mr. DROZAK. Well, if you take a T-2 tanker 20 years ago, she had a crew of 42 men from top to bottom, compared to today with the VLCC, which carries 12 times as much cargo as the T-2 with a crew of 22. Therein lies your difference.

Now, if you look at a container versus a conventional freighter ship with cargo booms the comparison is equally impressive. You will see that they are carrying 10 or 12 times as much cargo as the old Delta Line cargo ship used to carry.

Automation and high technology have done a job out there in reducing crew sizes.

Senator LONG. And what would be the number of men aboard one of those ships as compared to the way it was, say, 20 years ago?

Mr. DROZAK. Twenty-one men.

Senator LONG. Is it still 21 or less than that now?

Mr. DROZAK. No, it is 21 top to bottom now. It could get down as low as 18.

Senator LONG. But with approximately the same number of men, you are moving ten times as much tonnage, is that it?

Mr. DROZAK. Well, with 50 percent less than what we had on that conventional ship.

Senator LONG. Fifty percent less?

Mr. DROZAK. Fifty percent less crew, we are moving ten times the cargo on the new modern ships.

Senator LONG. So actually the cargo is 20 times per man-hour, the man-hour per cargo is 20 times as much.

Mr. DROZAK. That is about right.

Senator LONG. That is a big increase in productivity.

Well, I personally happen to think that the answer to a great number of these problems is for people to work together, rather than the farmers up here fighting. And I think those who urge the farmers to fight against the merchant seamen, which certainly does not help either one of you, I do not think—and I would rather have the farmers fighting the merchant seamen than one group of agriculture fighting another group of agriculture and all the rest of it.

What we really need is to get people to work together for the mutual advantage of all, because the farmers are getting the worst of it, you are getting the worst of it. And what I would like to see is a program that helps all of you. And if it means we have got to pay a little bit more for the product, so be it as far as this Senator is concerned.

Mr. DROZAK. Well, Senator, we have made every effort in attempting this last round of cargo preference to establish and work together with the farmers. But I do not think we understand what we are talking about. The cargo that we were fighting over was give-away cargo. It is not the product that the farmer is producing out there, regardless.

The Government bought this cargo and the Government is giving it away, and the law said that a minimum of 50 percent of it should be carried on American flag ships. Altogether the farm commodities exported by the U.S. Government amounted to only 2 percent of all farm exports. So 98 percent of all of the farm products are going on whatever flag ship they may want to go on.

So the rates do not have an impact on it. But people have made that an issue, Senator, to divide two very important industries, in my opinion, that are very important to national security.

Senator LONG. Well, I am for you, Mr. Drozak, even if it does make some of my farm friends mad. But I think that they ought to be helping you and you ought to be helping them. I think that you are going to need a bigger combine that you have got, and if I can help you put it together I will.

Mr. DROZAK. Senator, we have an agreement now that we are going to go talk to each other before we go out and do something. At least we have gotten that far. I wish we could get that far with all the

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shipowners and shipbuilders on the basis of their issues. Maybe some day we will.

Senator LONG. Thank you so much.

Senator GORTON (presiding). Frank, thank you very much for being with us today.

The chairman is temporarily absent, but he has asked me to proceed, and I think the next group will be the shipyard group: Mr. Rice, Mr. Fernstrom, and Mr. Wells.

Senator STEVENS (presiding). My apology, Frank. I had to go get a telephone call.

We now have Mr. Lee Rice, president of the Shipbuilders Council of America; Mr. Allen Fernstrom, president and chief executive officer of the American Ship Building Company; and Paul H. Wells, president of Adventure Cruise Lines.

If it is agreeable, we will proceed in that order. Mr. Rice.

STATEMENT OF M. LEE RICE, PRESIDENT, SHIPBUILDERS COUNCIL OF AMERICA; H. ALLEN FERNSTROM, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AMERICAN SHIP BUILDING COMPANY, ACCOMPANIED BY GERALD MALIA, COUNSEL; AND PAUL H. WELLS, PRESIDENT, ADVENTURE CRUISE LINES

Mr. RICE. Thank you, Mr. Chairman. Mr. Chairman and members of the Subcommittee, the position of the Shipbuilders Council on a build and charter program as envisaged is S. 1885 can be stated simply: We strongly endorse the program as a potential bridge between the current distressed state of our industry and the awaited progressive, well structured national maritime policy required by the nation's defense. Our lengthy statement details this position and urges that legislation to authorize the build and charter program be uncomplicated and flexible, while providing legitimate protection against unfair competitive advantage. Above all, authorizing legislation must be enacted as quickly as possible.

This is my fourth hearing on this issue and I would like to make some comments as an overview.

Our Nation must learn to better benefit from its experiences. Particularly, it must translate important lessons between complex and seemingly unrelated occurrences.

The management of complex undertakings requires that the efficacy of the system be continually monitored and tested as to the effect of both subtle and major changes in its physical components and in its human and philosophical elements. Achievement of defined or definable objectives which chart the course of our endeavors must be assessed both as to short term gains and long term risks and effects. These fundamentals of management apply both to space shuttle development and operation, as well as to national maritime policy formulation and execution.

There is a lesson to be learned in regard to build and charter.

Mr. Chairman, I have devoted a significant part of my professional career to the development of advanced rockets and missiles and complex management systems which ensure efficient functioning of man-safe missile and space systems. Upon analysis, startling parallelism becomes evident, between the findings of management system failures and the consequent disaster which the nation has experienced in the space shuttle program and the development and execution of a national maritime policy. Fortunately, the national disaster which parallels the Challenger loss, but is portended by current maritime policy, is yet to occur. I submit, however, that if it occurs it will pale in importance the Challenger losse.

From a possible litany of parallels two have been chosen. The first is a matter of ethical responsibility and common sense. In the space shuttle program, the persons placed most at risk to loss of their lives, the astronauts, were not given adequate information regarding engineering and testing details of the meaning of the warnings of risk which had been developed by experts within the shuttle development groups sufficient to allow independent assessment by the astronauts of the acceptability of risk either before or during the launch sequence.

As to national maritime policy, the persons placed most at risk to loss of their lives, the marines and other armed service personnel who require support from the maritime industry in a national emergency, have not been given full knowledge as to the industry's ability to carry out the difficult tasks on which they must rely or the warnings of deficiencies expressed by experts. Nor are those most at risk allowed to have: (1) the ability or the opportunity to critique the capability of others beyond their control on whom they must and are required to rely and (2) a mechanism through which they can sound an alarm when their and the nation's risk become in their professional judgment unacceptably high.

The second parallel is a stark warning of risk and highlights governmental management shortcomings.

Testimony and documents produced in the aftermath of the Challenger loss show there existed a substantial record of warning that the solid rocket motor case seals presented a high risk of disastrous launch failure unless engineering changes were made.

These warnings came from private industry and from within the National Aeronautics and Space Administration bureaucracy, both in writing and in numerous conferences. Yet the NASA management system was able to choose to subdue, ignore, and subsume the warnings and produce and sustain a "We're not worried, therefore all is okay" response. Shockingly, the most senior NASA management was never informed of the warnings or of the importance in an understandable way, if at all. Further, the inspector general system, intended to alert senior Administration executives and the Congress of the existence of such problems, failed to do so.

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There is a parallel in maritime policy development, eand execution. Numerous industry studies disclose and several internal warnings have arisen within the government bureaucracy which indicate maritime assets are inadequate and unacceptably high risks result from failure to solve the problem of providing adequate sealift, shipbuilding and seagoing labor capability and capacity.

Further, private industry experts who have strived to fully develop the dimensions of the problem and to provide constructive criticism and show errors of fact, interpretation or logic contained within governmental analyses which mask the problem are ignored. Their honest views are regarded as the utterings of special interest groups unworthy of audience, unimportant and unwelcome.

The current series of hearings on build and charter legislatiion have established that the Office of Management and Budget, who at best can be described as inexpert in maritime matters, have been able to subdue, ignore, and subsume the warnings of professionals and the voice of disagreement. Additionally, it is highly probable that even within the Department of Defense senior management has not been made fully aware of the depth of the maritime problem and of the pressing need for its solution. Thus, the Congress, the public, and the most senior executives of the Administration are denied information vital to the performance of their responsibilities.

The failure of the Administration to even nominate the private sector members to the Commission on the Merchant Marine and Defense created by the Congress in the summer of 1984 to specifically address the maritime problem is yet another example of the executive bureaucracy blocking activities viewed as threatening to pronounced dogma. As a consequence, efforts to constructively deal with the problem in the national interest are thwarted.

Mr. Chairman, I hope these brief comments are helpful and that they highlight particularly grievous errors in the assignment of responsibilities within the government bureaucracy. It is apparent that efforts of this Subcommittee in enacting authorizing legislatiion for the build and charter program are hampered by these errors.

Thank you.

[The statement follows:]

STATEMENT OF M. LEE RICE, PRESIDENT, SHIPBUILDERS COUNCIL OF AMERICA

I am M. Lee Rice, President of the Shipbuilders Council of America. The Council is the national trade organization which represents principal shipbuilders, ship repairers and the supporting suppliers who provide equipments, materials and services to these industries. A listing of the membership of the Council is attached as Appendix A.

Mr. Chairman, as you know, the Shipbuilders Council has consistently supported a "Build and Charter" program as envisaged in S. 1885 as an effective method for providing interim support to the American maritime industry, and industry vital to the nation's welfare. Under your guidance and leadership, "Build and Charter" has become the most likely legislation to provide near term support for our besieged industries. Your correctness and that of this Subcommittee in supporting such a program has been demonstrated by the fact that the maritime assets of the nation: namely, operating ships, functioning shipyards and men at sea, continue to decrease. In our view, the security of the nation has been jeopardized by inaction. We continue to decry the lack of attention being given to this important problem by the Administration.

The Council recently organized and led a briefing for LTGEN Alfred G. Hansen, Director, J-4 Directorate of Logistics, of the Joint Chiefs of Staff. The briefing examined information developed by industry experts regarding the following:

The U.S.-flag liner fleet both international and domestic,
The Effective U.S. Controlled fleet,
The U.S.-flag tanker fleet both international and domestic.
The NATO allies dry cargo fleet,
The U.S. government controlled operating and reserve fleets, and
The shipbuilding and ship repair industries.

The data, complied for the briefing by industry experts, showed in each of the categories studied that the availability and capability of assets are in varying degrees of decline. More importantly, it was the overall view of the experts that, absent a stable promotional maritime program in the United States, it is not possible to accurately predict the capability level of the fleets or the shipbuilding industry by the end of the present decade. It was universal, however, that decline would occur (1) in the overall fleets and in the number of militarily useful units in these fleets, (2) the shipyards available to the nation, and (3) skilled manpower. It was also clearly established that the reaction of the government to the downward trend, adding ships to the reserve fleets, is at best acting to delay a dangerous decline in our capability to meet mobilization and shipping requirements. Indeed, as the size of the reserve fleet growers so do the requirements placed on the shipbuilding industry for mobilization, yet the shipbuilding industry is allowed to continue to decline.

At the January 17, 1986 briefing, the Shipbuilders Council stressed that the premise governing the Administration's position that Navy shipbuilding and ship repair programs provide adequate support to maintain the required shipbuilding mobilization base is derived from suspect data, based on highly optimistic assumptions, and faulty in its logic. Appendix B develops these points in detail.

The overriding conclusion drawn at the briefing was that our nation needs to: (1) increase the stock of militarily useful vessels available, (2) increase the usefulness of currently existing fleets, (3) maintain a vital pool of experienced and able seagoing personnel composed of U.S. citizens, and (4) maintain our shipbuilding and ship repair capabilities at adequate levels. To do otherwise is to risk failing in our doctrine of deterrence.

As mentioned earlier, a "Build and Charter" program is not the full or final answer to the problems facing us. In our judgment, however, it is an efficient means by which we can act now to prevent an unacceptable decline in the maritime industries. "Build and Charter" will provide help and needed assets in three of the four categories articulated above.

Unfortunately, there appear to be a number of opponents to a "Build and Charter" initiative in senior positions in the Administration. For example, some government officials contend that increasing the number of vessels in the government reserve fleets is more efficient and cost-effective than is "Build and Charter." This conclusion ignores the need to provide work for the shipbuilding industry and the need to provide continuing work and state-of-the-art training for seagoing personnel. These same critics discount the estimated annual $1 million cost per vessel to the government to maintain the ships in an ever-expanding Ready Reserve Force. Indeed, the planned Ready Reserve Force is now 110 vessels and, if the recently admitted shortfall of tanker vessels is satisfied, the Force will be required to be enlarged to 185 vessels. The added vessels above the current level of 70 vessels will

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require very substantial added costs; both for vessel acquisition and ongoing costs for readiness maintenance.

Others contend that since "Build and Charter" may not return 100 percent of the government's initial investment in the program, it is an unwarranted subsidy to a diminishing industry. Those people conveniently forget that in addition to charter hire payments to the government, charterers pay federal taxes as do the seafarers employed on the ships. These same critics blithely ignore the linkage between the maritime industry and the national security, and choose to believe that maritime assets will always be available from foreign sources in any emergency facing the nation. They ignore the lessons of history and choose instead to advance theoretical economic doctrines, which are dangerous to the national security.

Others contend that there will be no charterers of vessels constructed under a "Build and Charter" program and that the program will fall short of its full potential. Our analysis indicates that if the government builds vessels destined for dry cargo trades to the lesser developed countries, there is a high likelihood that the ships can have high military value and be chartered on a relatively long term basis. It is our understanding that the testimony of owners to be given at this Hearing will support that view. Our discussions with the Navy have confirmed that vessels of the type under discussion between shipbuilders and potential charterers will be highly desirable for military purposes. Moreover, the construction of vessels in the United States will have a positive impact on our balance of trade.

The Shipbuilders Council believes there are other classes of vessels which will find charter markets. For example, deck strenghtened RO-RO vessels, if built with commercial characteristics, can be chartered for use in the international car transport business. It is likely that they would be chartered for shorter periods than the vessels built to serve in the dry cargo trades because of the nature of that market. Even the Navy has acknowledged a need for product carriers to transport refined fuel. Finally, the possibility of passenger ships for the U.S. cruise market should not be dismissed.

A major negative factor overhanging the international and domestic shipping industries is the possibility of changes in U.S. tax law. Based on Administration proposals and legislation passed by the House of Representatives, it appears likely that major modifications affecting cash flow will be enacted into law, which could further handicap owners of U.S.-flag vessels as compared to their foreign competitors. Illustrative are the repeal of the investment tax credit and lenghtening depreciation schedules governing vessels. Thus, the fundamental premise of the Administration in that commercial forces will provide adequate numbers of sealift assets, bought abroad, is dealt yet another blow and in our judgment becomes an even more imprudent strategy.

Following enactment of new tax provisions which make U.S. operators even more disadvantaged, the charter of a government owned vessel will become much more attractive. This is true because the government would not bear the tax burden and thus not be forced to pass that disadvantage onto the charterer.

It is our understanding that the Navy may engage the Maritime Administration as its procuring and chartering agent under the "Build and Charter" program authorized by S. 1885. We agree that this method of management is workable. The Shipbuilders Council, however, strongly opposes any transfer of control of the funds to the Department of Transportation. Our opposition is based on the conviction that if this were to occur, the funds might not be used for the intended purposes.

None of us can predict with certainty what the international shipping markets will be beyond the near term. "Build and Charter" legislation must be as flexible and unrestrictive as possible with full consideration of the advantages and problems which could confront operators of the vessels built under the program. The Council believes that the trade and other restrictions included in S. 1885 are sufficient. This is especially true with respect to the language which prohibits a vessel constructed under the program to be chartered or sold for operation in the coastwise and intercoastal trades. We anticipate a good number of vessels meeting the objectives of the bill will be built and they can enter service and be productive without causing undue competitive disruptions. We project that approximately 13 to 18 vessels could be constructed under the program.

Is "Build and Charter" the final answer to the dilemma of how best to provide required maritime assets at lowest cost to the nation? No, it is not. Even after enactment into law of "Build and Charter" there will be much which remains to be done to insure that our nation has in place an effective and efficient maritime policy and program consistent with the requirements of national security. "Build and Charter" is only a positive first step—but it is an essential first step.

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In summary, the Shipbuilders Council strongly endorses "Build and Charter" and urges the support for the program by your colleagues on the full Commerce, Science, and Transportation Committee and in the Senate. This concludes my prepared statement. I will attempt to answer any questions that you may have.

Senator STEVENS. Thank you.

Mr. Fernstrom.

I am H. Allen Fernstrom, president and chief executive officer of the American Ship Building Company. I am accompanied by Gerald Malia from the law firm of Reagan and Mason.

We appreciate the opportunity to appear today to present American Ship's views on S. 1885, the build and charter proposal. The American Ship Building Company strongly supports legislation to establish the Mariner Fund, under which modern ships will be built to meet military sealift needs, the Navy will select the types of vessels to be constructed and these vessels will be available for military use.

Mr. Chairman, we hope that our comments and suggestions as to the provisions of S. 1885 will be of use to the subcommittee in its efforts to finalize this measure and to achieve realization of this important program.

S. 1885 will establish the military auxiliary revolving fund, to be administered by the Secretary of the Navy in consultation with the Maritime Administration. The fund shall be used only for the construction in private shipyards in the United States of merchant vessels capable of serving as military auxiliaries.

We believe there is a clear need for new militarily useful commercial vessels under American flags. Sealift support ships of all kinds, with modern technology for communications, navigation, and operations are vitally needed.

We now live in a computer age and maritime technology has taken full advantage of these developments. This technology needs to be emphasized in the American merchant marine.

Support vessels provide the lifeline of the combat fleet and enable our forces to be deployed at great distances for extended periods of time. The accomplishments of our shipyard in Florida over the last several years in the construction of product tankers for charter to the Navy is an important development in the industry, and I would like to take this opportunity to provide the Committee with a briefing on our facilities.

Our Tampa shipyard is one of the newest, most efficient in the world. We have recently invested over $60 million in new shipbuilding facilities in Florida. During 1985, we provided employment to over 2,000 persons in the Tampa shipyard.

We offer a complete ship construction, conversion, and repair facility, which utilizes the most modern ship construction technology in the world. During 1984–85, we completed construction of two new drydocks in which we built the T-5 product tanker for charter to the Navy.

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Each T–5 is designed to deliver 30,000 tons of fuel or other liquids worldwide, and they are strengthened to withstand ice in Arctic and Antarctic use. We are now completing a fifth ship of the T–5 series.

This program of five vessels will have been completed in a total of less than 3 years from the contract to the delivery of the final vessel. As a matter of fact, all five ships will have been delivered in a 10 month time period. These are modern vessels which enhance the Navy's ability to transport a variety of fuels to fleet installations and ships at sea by means of underway replenishment technology.

This is a unique feature of major significance to the military. The Tampa shipyard, under the leadership of its president, has implemented an innovative method of modular construction and advanced pre-outfitting to assure timely delivery.

In this program we also utilize CAD/CAM, computer-aided design and computer-assisted manufacturing, to speed up the cutting and assembly of steel plates. This is an advanced application of CAD/CAM for ship construction in the United States.

Our T–5 construction program has been unique in the U.S. shipbuilding history because time is of the essence in ship construction, considering cost alone. We initiated a program of sharing work with other yards so that maximum work could go on simultaneously in various yards and suppliers.

CAD/CAM therefore enabled us to cut dramatically the period usually required for shipbuilding. The T–5 forebodies were built by Avondale Shipyards and the deckhouses were built by Alabama Drydock. We have subcontracts with hundreds of companies in many states across the country.

We can report excellent results on our T–5 program, and we believe the Navy is very satisfied with this enhanced ability to move substantial cargoes of jet fuel and other petroleum products to the fleet. The four vessels which have been delivered were immediately introduced into service by the Military Sealift Command for naval operations.

We urge the Committee to ensure, by amendment to the bill if necessary, that the legislation will allow flexibility on the part of the Navy to have vessels which are built under this program eligible to be chartered to the Navy's Military Sealift Command. The Navy has the control over the type, size, and number of vessels to be built, and should likewise have the ability to have the actual use of the vessel, not just during hostilities, but during peacetime as well.

In the case of tankers, the Navy has traditionally chartered privately owned tonnage for an extended period in order to have long term reliability.

Mr. Chairman, American Ship supports the new build and charter program, and our comments and suggestions are submitted to the Committee in the hope of being of assistance in the effort to enact this program. We believe the new build and charter program will benefit our military, as well as all segments of the American merchant marine industry.

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It should provide much-needed employment and vessel construction work for U.S. shipyards, and assure that militarily useful commercial-type vessels are available to provide jobs to U.S. merchant seamen and provide ship operators with an opportunity to obtain modern and commercially competitive U.S.-built vessels.

We appreciate the opportunity to appear before you today to present our views on this bill. I would be happy to answer any questions you might have.

Senator STEVENS. Thank you very much.

Mr. Wells.

Mr. WELLS. Thank you, Mr. Chairman.

First off, I want to clarify. I am not a ship builder; I am a ship operator.

For the record, my name is Paul Wells. I am president of Adventure Cruise Lines. I will summarize the statement I have submitted for the record.

I am very pleased to have the opportunity to comment on S. 1885, with particular reference to the potential I see to revitalize the U.S. flag passenger vessel fleet. Since 1972, I have been associated with companies operating foreign flag passenger ships and I am thoroughly familiar with the operations of passenger cruise vessels.

As I am sure the members of the subcommittee are aware, no new passenger vessels have been built in the United States in over 30 years. Adventure Cruise Lines has been working to put together a project to design and build a competitive U.S. flag passenger vessel in the United States, to be manned by Americans and operated in various American cruise trades.

We have designed a passenger vessel that can be built in the United States at a competitive price. We are certain that our design could be modified to make it suitable as a troop transport in times of emergency, carrying approximately 3,000 troops.

As this committee knows, the Title XI program is proposed to be terminated and the tax reform bills substantially decrease incentives for investment in capital assets. I support the Title XI program and hope it will not be terminated.

If it is terminated, however, this program could become the only vehicle for building large commercial ships in this country. The program presents a unique opportunity to take advantage of the demand for additional ships in the foreign and domestic cruise trades and also fill the military's needs for emergency troop transport capacity and a substantially lower cost.

Special considerations apply to passenger vessels, however. Vessel design must be geared to specific markets. The vessels must provide a pleasant environment along with good service and entertainment, while being competitive in both capital and operating costs.

All construction design and engineering should be done principally by the private sector, in cooperation with the Navy. But the entire project, including vessel pricing for proposed operation, must be developed on a coordinated basis.

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In my view, this is the only way to ensure commercial viability and still satisfy the military requirements. Certain of the concepts in S. 1835 are in conflict with these requirements.

For example, bidding by operators for the completed vessel is inconsistent with the joint Government-cruise operator project approach which I believe is essential. In addition, the proposed limitation to operate in foreign commerce should not apply to passenger vessels, since such vessels must have the flexibility to react quickly to changes in markets in order to remain competitive. The inequity that would result from Navy-built vessels competing with vessels built at full domestic cost could be eliminated by assuring the charter rate in domestic trades reflects full domestic costs to build a vessel of comparable size meeting industry standards for outfitting and speed.

Charters should also contain an option to purchase after a period of time, to provide an added incentive. This option should be at a price reflecting domestic costs if the vessel is to be operated in coastwise trade.

As I understand the program, once the vessel is chartered or sold to an operator the operator assumes all financial operating risk. These risks are substantial in this case of cruise operations. Large investments must be made to set up an organization to advertise and book passengers. In the case of charters, the operator must also guarantee payment of charter hire for some period.

In light of these risks, I believe the provision for sharing profits in excess of 10 percent is inappropriate.

Finally, the bill provides that any charter can be terminated without cost to the United States in a national emergency. This would result in unduly harsh consequences to the cruise operator.

Both the direct and indirect expenses incurred in cruise operations are far more substantial than those arising in other maritime operations. Cruises are advertised, marketed and booked well in advance. The travel agents' commissions, advertising commitments, and advanced bookings can result in substantial losses if the cruise is canceled.

There must be, therefore, some formulation to reimburse the operator for those expenses in the event of charter termination.

Finally, it should be clear that the insurance to be provided would be consistent with industry standards.

This Committee and program have our wholehearted support. I wish to express my interest in participating in this program, subject to the comments which I have made. We would be happy to provide specific recommended changes in statutory language should the Committee so desire.

Thank you.

Senator STEVENS. Thank you very much, Mr. Wells. We appreciate your taking the time to join us.

Mr. Rice, I appreciate the comments you made, the philosophical comments in particular. My young friend here and I have been wondering how we got where we are with the lack of active support for the legislation. I was convinced last year that if we could have the money

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standing there to show that it was available, that perhaps there might be more of a coalescing of support for the concept.

But that has not happened in the Senate, obviously. I am at a loss to even ask a question about it, but it just seems to be there is something lacking in the awareness of the plight of the nation's dependence on a struggling merchant marine industry. And as I said, I do not have any questions.

I admire your statement and I think your analysis is a good one.

Mr. Fernstrom, your T–5 process is an interesting one and I understand that you did some real innovative work in computer design. Do you think, with the advent of technology, that we will have a restoration of the competitive position of the U.S. shipyards vis a vis foreign shipyards?

Mr. FERNSTROM. Senator, that is a very complex question, the reason being is that it has many facets to it. We believe at Tampa Ship, which is a wholly owned subsidiary of American Ship, that with our facilities and with the innovative things that our people have done in the shipyard, that we can compete on a productivity basis with other yards in the world.

So then it becomes a question of wage scales differences and the cost of the materials.

Senator STEVENS. How about taxes?

Mr. FERNSTROM. And taxes, and any types of tax or subsidy type situation.

So the problem we have is we can work on the areas that we have under our own control, and that is providing facilities, up to date facilities, up to date technology to do the job, and provide the necessary training and incentives to our workers to be able to produce on a competitive basis with other yards in the world. But we cannot control international wage rates, or we cannot control costs of materials that could be procured.

Senator STEVENS. I thought you might comment on one provision of this bill that requires that 50 percent of the cost of all machinery be related to U.S.-manufactured goods, and the relationship of that to the whole problem of obtaining the new low-speed diesel engines. Have you looked at that provision and how it might relate to the question of the machinery costs associated with conversion to diesel engines?

Mr. FERNSTROM. You could build these, the T–5 tankers, as they are being built today, with slow-speed diesel engines, which are—the only source in the world at the moment is foreign, being produced in Japan. You could build these vessels and still meet the 50 percent of foreign content if you just included the diesel engines.

That would preclude you from any other foreign materials going into the vessel, which would increase the overall cost of the vessel.

Senator STEVENS. Is there any progress being made in this country in producing diesel engines that are available, at a comparable price, to your knowledge?

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Mr. FERNSTROM. Unless somebody else would like to comment, not to my knowledge.

Senator STEVENS. Thank you very much.

Again, MR. Wells, I do not have any questions about your statement. I appreciate that you have taken the time to participate in the hearing. I understand what you are saying about the relationship of this bill to Title XI.

Senator Long?

Senator LONG. Mr. Rice, the analogy you drew between the disaster that happened in the space program and the Challenger and the type disaster that could conceivably happen for failure to have proper and adequate merchant marine was very impressive.

Now, you concluded by saying: "The failure of the administration to even nominate the private sector members to the Commission on Merchant Marine and Defense created by Congress in 1984 to specifically address the maritime problem is yet another example of the executive bureaucracy blocking activities that are viewed as threatening to pronounced dogma."

Now, I did not know until you said it here that we provided for this Commission on the Merchant Marine and Defense to study this problem, and that the administration had not even nominated the private sector members. Now, I know a little bit about the Government, you know, having been it it all my life. I know enough. I say, my father was running for office the day I was born, and that was 67 years ago.

So I have been in this job for 37 years, and so that I know enough about some things that happened in Government to know that that does not happen because the President wants it to be that way. That just happens because someone in the executive branch is falling down on his job.

I do not quarrel with the President at all doing the job the way he is doing it. If I had the job, that is how I would like to do it, the same way he is doing it. But when you rely on the staff--and a man with that job has to rely on staff, does he not?

Mr. RICE. Yes, sir.

Senator LONG. So when you rely on the staff, and then something goes flat damn to hell, like occurred with the Challenger, here he is and things going up in space, how beautiful, how lovely—boom, it blows up in a great big disaster.

And the only good thing about that is it could have been worse. It could have been something involving a great deal more lives even than those courageous Americans involved.

So that someone down there did not do his job. And I know the chairman of this subcommittee is willing to do his part. And I want to volunteer, Mr. Chairman, to do my part to help you in that, so we can get behind these people.

Now, who the hell is it down there that has the responsibility for presenting the President some names to name to this Commission? You have got enough here in the room to nominate from the civilian side of it. Just say, let us get some names up here to do this job and lay before

the President some recommendations, to alert the people to what the problem is.

Now, the other big aspect of your problem and the rest of it, I see it as the same thing I told Mr. Drozak. We need to get people together. It has been my good fortune to draw the support of people in your industry in my state, insofar as we have any shipyards. They seem to appreciate my merit and I appreciate their merit. They are very fine people and I do all I can to help them.

But that Seafarers Union is a very good union. From the point of view of a guy that runs for office, there is a fine good bunch to have for you, I can tell you that from 37 years experience.

I one time sat down in New Orleans and I went to a meeting that I thought was a convention of Seafarers. It turns out there were a whole bunch of unions there, and I made the statement that if I had the choice of which union I wanted, that I would be willing to take the Seafarers and the other guy could have all the rest of them.

Now, that's saying a lot. But the Seafarers in New Orleans have been extremely effective, and they just have done all they could do to help you, and in a completely proper and ethical way.

So you need them and they need you, and also we need the ship operators. And frankly, we need a bigger combine than that. If I can help you put it together, why, I will do what I can, because I just feel like there are people all over this country that are suffering, and a lot of it is because they have not worked together.

Just like our farmers. You go out there and there they are all broke. They are losing their land, being foreclosed on. There is about 100,000 acres, you know, that they would like to sell in foreclosure right now in Louisiana, just to mention one State.

And it need not be that way, but people need to work together to keep that sort of thing from happening to them, not by fighting somebody who ought to be on their side. It is by working with people who ought to be on their side.

Thank you for coming here, and we appreciate your testimony, all of you.

Senator STEVENS. Thank you very much. We will try to get the answers to your questions, Mr. Rice.

Next, the next group is: Mr. Shapiro, vice president and general counsel of Apex Marine; Robert Thompson, director of Government affairs, Moore McCormack Resources; and James McGregor, vice president, Ocean Shipholdings.

Gentlemen, we are pleased to see you. Mr. Shapiro, you are first on my list. If that is agreeable with you all, we will proceed that way.

STATEMENT OF PHILIP J. SHAPIRO, VICE PRESIDENT AND GENERAL COUNSEL, APEX MARINE CORPORATION, ACCOMPANIED BY THOMAS MILLS, COUNSEL; ROBERT THOMSON, DIRECTOR OF GOVERNMENT AFFAIRS, MOORE McCORMACK RESOURCES, INC., ACCOMPANIED BY STEVE SILVER, COUNSEL; AND JAMES P. McGREGOR, VICE PRESIDENT, OCEAN SHIPHOLDINGS, INC.

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Mr. SHAPIRO. Thank you. Good afternoon.

I am Philip Shapiro, vice president and general counsel of Apex Marine Corporation. Behind me is my counsel, Thomas Mills from Washington.

Mr. Chairman, as I testified earlier, we wholeheartedly support the build and charter initiative. I think it is important, however, that I reiterate our vital concern that the vessels built under this program be strictly limited to sale or charter at prices of charter rates reflecting nothing less than the world price for new construction of the same vessel at the time the vessel is delivered from a U.S. shipyard.

Earlier I suggested a specific formula for giving effect to that concept. Other than that, I would like to add our voices to those who see a vital national defense requirement for new, modern, handy sized product tankers with coated tanks.

I might also suggest that this program be utilized to develop a U.S. PCC vessel fleet for the carriage of Japanese automobiles to the United States, with strengthened decks and moveable 'tween decks.

We see no possible way, given the existing and projected market conditions, that the private sector will build any of these product tankers, with the exception of an occasional new building for proprietary use. The current proposal to add a 10 percent surcharge to those imported petroleum products not carried in U.S. flag vessels will indeed create a market for these new product tankers.

Given the unquestionable national security need, build and charter appears to us to be the perfect solution to the problem. A number of new ships of this class could be built under the program for the foreign trade. The Berger Group would undertake to charter these ships and operate them in a foreign trade if the program were so structured as to yield a commercially competitive charter rate.

That is to say, the delivered vessel must be able to deliver petroleum products at prices charged on the world market within the same time its commercial competitors can deliver it, and be able to do so under the same physical and environmental conditions.

Unfortunately, that means that the full domestic cost cannot be reflected in the charter rate. Some of it has to be defrayed by the Government. The cost is justified, however. Our Navy maintains a sea lane strategy, and I note that the Navy is contemplating building 100 new attack submarines, at the approximate cost of $1 billion apiece.

In that context, $850 million does not seem very much money at all to spend for vessels, indeed vessels vital to our national defense, to ply the sea lanes, given that we are going to spend $100 billion in new money to protect them.

As to the structure of the bill, we have no doubt that the bill might work in several different ways. Our own opinion is that to bid the ships out on a competitive basis for construction and then separately bid them out for sale or charter is not the most efficient manner to administer the program.

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We think it would be more economical to package the new buildings as a project, matching up vessel design specifications, shipyards, and operators. The Navy and the Maritime Administration should approve of the vessel type and its national defense features. The package should then be competitively bid so that the end product will be delivered at the cheapest cost, be a commercially viable asset, and still satisfy all of the defense requirements. We would be very pleased to work with your staff to develop the specifics of such a proposal.

That concludes my oral statement, Mr. Chairman. I would be pleased to answer any questions.

[The statement follows:]

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STATEMENT OF PHILIP J. SHAPIRO

S. 1885

I am Philip Shapiro, Vice President and General Counsel of Apex Marine Corporation, which operates 14 U.S.-flag vessels in domestic and foreign commerce and has 2 vessels under construction for delivery and documentation under U.S.-flag. Captain Leo V. Berger is the principal owner of the companies which own the vessels which Apex operates, and they are collectively known informally as the "Berger Group."

As I testified in the earlier hearing, the Berger Group wholeheartedly supports the build and charter initiative. I want to reiterate, however, the vital concern our group has that vessels built under this program be strictly limited to sale or charter at prices or charter rates reflecting nothing less than the world price for new construction of the same vessel at the time the vessel is delivered from a U.S. shipyard. I ask that our earlier testimony with its specific recommendations, which I have attached to my written statement, be included in the record of this hearing.

I would like specifically to add our voice to those who see a vital need for small, handy-size product carriers with coated tanks. I know the military has grave concern over our lack of logistical capacity in this area. Very few handy-size product tankers have been built in this country largely because old, inefficient tonnage—primarily jumboized T-2's—have continued to overhang the market. Despite the inefficiency of those old clunkers, the dramatically higher capital costs of new tonnage led to a market result that could not justify new tonnage. The Port and Tanker Safety Act of 1978 has since forced much of that tonnage to the scrapyard, although an alarming number still continue to operate at reduced capacities. Accordingly, without additional restrictions, it is unlikely that the domestic market will provide any incentive for the construction of new product carriers in this class.

The Berger Group believes that build and charter is the perfect solution to this national security need. A number of new ships of this class could be built under this program for the foreign trade. Our group would undertake to charter such tonnage and operate it in the foreign trade if the program were so structured as to yield a commercially realistic charter rate that is internationally competitive.

With respect to the structure of the bill, we believe it important that any final legislation be geared to the commercial bottom-line. Any vessel built by the government under this proposal must be able to deliver petroleum product at the price charged on the world market, within the time its commercial competitors can deliver it, and do so under the same physical and environmental conditions. That means that the full domestic cost cannot be reflected in the charter rate. Some of it must be defrayed by the government. And, while operating efficiencies from new modern tonnage, together with the concessions being made with respect to manning, wages, and benefits by maritime labor, make our vessels generally competitive with equivalent industrialized nations, our operating costs may not be low enough to compete hear to head with ships manned by third world crews. That remains to be seen at the time of the vessels' actual deliveries.

Notwithstanding those facts, this program will yield national defense assets at a cheaper relative cost than any other in the defense budget. Your bill will purchase "more bang for the buck" because a great portion of the cost will be covered by commercial operations.

Again, Mr. Chairman, this committee has our compliments, our support, and our undertaking to help bring about the result intended by this program. We would be happy to provide specific recommended changes in statutory language should the committee so decide. I would be pleased to answer any questions.

S. 1832 AND S. 1833

I am Philip Shapiro, Vice President and General Counsel of Apex Marine Corporation, which operates 16 U.S.-flag vessels in domestic and foreign commerce and has 3 vessels under construction for delivery and documentation under U.S. flag. Captain Leo V. Berger is the principal owner of the companies which own the vessels which Apex operates, and they are collectively known informally as the "Berger Group."

We wish to compliment Senators Stevens and Inouye on developing a program to support the United States flag merchant marine engaged in foreign commerce and in general, subject to a few comments, we wholeheartedly support the effort represented by this legislation.

It is vitally important to our company that vessels built under this build and sell or charter program be strictly limited to sale or charter at prices or charter hire

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reflecting nothing less than the world price for new construction of the same vessel at the time the vessel is delivered from a U.S. shipyard. Our companies have made very substantial capital investments in vessels for the foreign commerce of the United States, principally in the cargo preference trades. We cannot afford to see that investment undercut by new ships constructerd or charted at less than the world price of constructing a new vessel. Accordingly, we recommend that in S. 1832, the Committee delete the following language from line 8 through line 10 on page 3: "taking into account financing terms and relative delivery times available from United States and foreign shipyards".

It would be virtually impossible accurately to translate financing terms and delivery time into reduced capital cost. We fear that in its enthusiasm to sell these vessels the Navy may reduce the price significantly to account for such amorphous conditions. In addition, since the Navy is building the vessels and designing the vessels there is really no delivery period: the purchaser will presumably be buying a shelf item from the Navy. Since financing terms are not available under the statute, the company purchasing the vessel would be free to obtain whatever market financing terms were available to him.

In addition, we suggest that in S. 1832, section 1401(d) begining on line 23 of page 2, the period be changed to a comma and the following language be inserted: "but in no event for an annual charter hire equal to less than 16½ percent of the foreign cost of constructing the vessel in a foreign shipyard at the time the vessel was delivered to the Secretary."

The same language should be inserted at the end of section 1401(d) in S. 1833 beginning on line 8 of page 3 where the period should be changed to a comma and quoted language inserted.

The 16½ percent is intended to represent a 4 percent annual depreciation charge and 12½ percent annual interest. When a vessel is chartered to an operator it amounts, in effect, to the loan of the capital asset, and the bareboat charter hire should at least reflect the annual depreciation on the asset plus an interest factor for the loan of its capital value. The 4 percent represents annual depreciation based on a 25-year life, and 12½ percent is an estimate of the long-term interest rate which would be applicable under Title XI financing or similar financing.

With these modifications, our companies wish to lend our support to the efforts of the Committee to take one step toward rejuvenation of the merchant marine engaged in foreign commerce.

Senator STEVENS. Thank you very much.

Mr. Thompson.

Mr. THOMSON. Thank you, Mr. Chairman. Mr. Chairman, members of the subcommittee:

My name is Robert Thomson. I am director of Government affairs of Moore McCormack Resources of Stamford, CN, and I am also general counsel of Moore McCormack Bulk Transport, the Corporation's operating subsidiary in the oceangoing bulk trades.

With me is my counsel, or our counsel, Mr. Steve Silver, who is sitting behind me on the left.

I thank you for the opportunity to remark upon S. 1885, a bill to institute a build and charter program for merchant vessels capable of serving as naval and military auxiliaries in time of war or national emergency.

And with your permission, Mr. Chairman, I would like to read my statement in its entirety. It is only about 2½ minutes long.

Senator STEVENS. Please do.

Mr. THOMSON. Moore McCormack operates three 39,000 deadweight ton Coronado tankers in the international petroleum trade. All three are currently operating in the spot market, primarily out of the Caribbean. All three were built with construction differential subsidy and were

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delivered at 6 month intervals from December of 1975 through January of 1977.

Moreover, all the vessels receive operating differential subsidy pursuant to a 20-year contract with the Maritime Administration. Given their handy size, their high maximum speed, and other operating characteristics, the ships are ideally suited for employment by the Navy, although, as noted above, they are currently operating in the commercial market.

The bill which you are considering today, if signed into law, would have more direct impact on Moore McCormack than on any other company operating U.S. flag ships. In response to questions at the subcommittee's November 15 hearing, and of course again today, Assistant Secretary Pyatt testified that the vessels most likely to be built under a build and charter program would be handy sized product tankers. I believe he was even more positive about that today. He said that would be the ships that they would seek to build.

Under the terms of S. 1885, these new ships would compete directly in the international trades now served by Moore McCormack. Of the relatively few U.S. flag handy sized tankers built specifically for the international trade, only the three vessels operated by Moore McCormack are now actually operating in that commercial market.

That market has not proved to be a profitable one. In 1980, tanker spot rates for handy size clean product tankers in the Caribbean to the U.S. East Coast trades were approximately Worldscale 275. Today, such rates are around worldscale 100.

Even with operating differential subsidy, rates of this magnitude are not profitable for U.S. flag handy sized tankers. The reason for the precipitous drop in rates in the last 5 years is obvious. The January 1986 edition of Lloyd's Shipping Economist notes that for tankers in the 10,000 to 40,000 deadweight ton class, supply exceeds demand by 16 percent.

The figure is 24 percent for ships in the 40,000 deadweight ton to 150,000 deadweight ton category. This surplus has a disproportionately greater impact, of course, on U.S.-flag tankers, since even with operating differential subsidy we seem to be among the highest cost operators.

Our conclusion from Moore McCormack's standpoint is that the construction of even a few product tankers under the proposed build and charter program, let alone the dozen or more ships that could be built with the money available, would have a disastrous impact on Moore McCormack.

Having said that, the subcommittee should not conclude that our company, Moore McCormack, opposes S. 1885, provided our unique problem is addressed. We realize that your decision on this legislation must necessarily be based on the defense needs of our country and the prospects for survival of our shipyards and the U.S. maritime industry in its entirety.

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Nor should anything we have said to date be taken out of context and used as an argument against the build and charter program. Tankers constructed under build and charter may have far different economics than do our vessels.

In the main, we rely heavily on the sense of fairness that the subcommittee has always maintained in its sometimes frustrating efforts to do positive things for the industry. Moore McCormack is certain that a reasonable solution can be worked out with the chairman, subcommittee members, staff, and other concerned parties in discussions that we earnestly hope will follow.

We believe if we work with you and your staff, a solution can be found that does not add to the federal deficit over the long term and serves the basic purposes of S. 1885.

In closing, and on behalf of Moore McCormack, please let me commend you, Mr. Chairman, your staff, and other members of the Committee, for all the hard work that has gone into this legislative project so far. We are confident the fine tuning necessary to deal with our particular concern is minor when compared to the results that we all hope will emerge.

Thank you.

Senator STEVENS. Thank you very much, Mr. Thomson.

Mr. McGregor.

Mr. MCGREGOR. Thank you, Mr. Chairman.

I am James P. McGregor, vice president of Corporate Development and Marketing for Ocean Shipholdings, Inc., of Houston, TX. I would like to thank you for inviting us to present our views in this hearing today, and I would also like to thank you for your consistent support of this legislation.

With your permission, I would like to ask that my written testimony be entered into the record, and in the interest of time, in the time available I would like to address some issues that are not in my written testimony, but I believe are relevant to the Committee.

Senator STEVENS. We would be pleased to do that.

Mr. MCGREGOR. Thank you, Mr. Chairman.

I would first like to say, Ocean Shipholdings supports this legislation. We believe that there is a critical urgency to get on with the building of U.S. flag petroleum product tankers, as stated by the Secretary of the Navy this morning and in his statements before the House hearings last Thursday.

We presently see a serious shortfall developing for U.S. flag product tankers. And before I proceed, I would like to draw a distinction between the handy sized product tankers that we are talking about and the general petroleum tanker market. On the basis of the size of the vessels, we are generally talking about handy sized tankers being anywhere from 25 to let us say 60,000 deadweight ton, tankers that are capable of carrying refined petroleum products.

In this segment of the U.S.-flag tanker fleet, we are looking at a rapidly dwindling fleet to begin with, as the older generation of steam-driven tankers, many of which were built during World War Two and

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were then later jumbo sized in the 1960's, are going off to scrapyards. We are also seeing an increasingly obsolete U.S.-flag tanker fleet due to the fact that the U.S.-tanker fleet primarily consists of steam turbine tankers. These vessels presently are not capable of competing in the foreign markets, and the reason is primarily due to the relative fuel consumption of these ships.

There are several factors that we see presently that are impacting the demand for U.S. flag tankers. I have already mentioned the changing fleet composition through ship scrapping.

One other factor that we see is the recent cancellation of the Trans-Gulf Pipeline Project, which would have carried clean petroleum products from the U.S. Gulf (New Orleans area) down into Florida. In addition to that, we have the requirements of the U.S. Port and Tanker Safety Act that tankers install segregated ballast tanks.

There is one other factor that we see affecting the demand for U.S. flag product tankers now, and we expect that it will continue this way in the foreseeable future. That is the recent changes in the crude oil pricing and supply situation worldwide.

As the price of crude has fallen over the last several months, we have noticed that the demand for product tankers has increased for foreign flag product tankers (to begin with). The reason for this is that as the pricing differentials for crude oil around the world change and get out of line with the way they have been able to adjust themselves through natural market forces, opportunities arise for oil traders and oil supply companies to buy petroleum products and to ship those products to terminals around the world in trade patterns that are highly unusual, given the type of supply patterns that we have been seeing historically.

For example, recently I made a list of some ship charters that I took out of the *Journal of Commerce* publication of tanker charters, and we see clean petroleum products, moving once again from Indonesia to the U.S. Atlantic coast. We see ships that are chartered to move clean products from the Indonesia area to Europe again.

We are seeing—and I am just looking down a list, a summary list of typical ship charters—products being moved from the Black Sea to West Africa.

We see that this situation is analogous to the type of increase that would be placed on the demand for petroleum product tankers in the time of a global emergency.

An example in the U.S. flag tanker fleet of the increasing and urgent shortfall of Jones Act tankers was seen last Thursday when the Military Sealift Command was forced to charter a U.S. flag tanker to carry military fuels from the U.S. Gulf to the U.S. Atlantic Coast at rates that are higher than they paid for that movement over the last 3 years.

We are also aware that there will be increasing problems with the availability of U.S.-flag tanker tonnage, not 5 years from now, but within the next several months. And we have gained this information from recent meetings that we have had with the Military Sealift Command.

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Therefore, we are primarily concerned with the worldwide national security interests of the United States and the need for petroleum product tankers. We have had many discussions with the Navy about the forecast that was referred to, the DOD forecast, that forecasts a critical shortfall of 75 handy sized tankers within 5 years.

And our company is interested in this legislation, Mr. Chairman, primarily for the reason that we see it as a very important infusion of capital into the U.S. merchant marine industry.

I would like to say that we have also submitted some suggested language that would enable the Secretary of the Navy to make a determination of the economic viability of any shipbuilding projects that are presented under this program.

That is a summary of the issues that I wanted to raise here in addition to what is in my written testimony. And again, Senator, I wanted to thank you for inviting us here to testify before this Committee, and I want to thank you for your continued support of this legislation.

I would be happy to answer any questions you may have.

[The statement follows:]

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STATEMENT OF JAMES P. MCGREGOR, VICE PRESIDENT, OCEAN SHIPHOLDINGS, INC.

Mr. Chairman, Members of the Subcommittee: I am James P. McGregor, vice president, Corporate Development and Marketing, Ocean Shipholdings, Inc., Houston, Texas.

We appreciate your invitation to appear here today to answer your questions and to present our views concerning S. 1885, the "Build and Charter" proposals.

Ocean Shipholdings is an operator of U.S. flag petroleum product tankers. As a ship operator, we believe that economically viable ship projects will be presented to the Secretary of Navy upon enactment of "Build and Charter" legislation. In determining the future comercial utility of vessels constructed under the fund, it is important to consider the dynamics of the shipping market in which the vessels will trade. Specifically, we see many opportunities for U.S. flag petroleum product tankers constructed with the most efficient propulsion technology available today to compete in future U.S. foreign trade. Also, we believe it is possible, under this program, for a vessel to effectively compete in that foreign market without receiving any direct operating subsidy.

In order to clarify our position regarding the legislation, I would like to take this opportunity to describe our primary business interests.

In 1982, one of our subsidiary companies was awarded a long term "Build and Charter" contract by the U.S. Navy, Military Sealift Command, for five 30,000 deadweight ton petroleum product tankers, commonly referred by the Navy as T-5 class tankers. Four of these tankers already have been delivered and one is still under construction at Tampa Shipyards, Inc., a subsidiary of The American Ship Building Company. The vessels will be used by the Military Sealift Command to carry DOD cargoes in worldwide trade. We charter those tankers to Military Sealift Command under time charter contracts which provide that we crew, provision, insure, maintain and generally manage those vessels. We are pleased to report that those tankers are operating efficiently for the Navy.

We also operate four 35,000 deadweight ton U.S. flag tankers for an independent shipowner. These vessels were built with the help of construction differential subsidy and receive an operating subsidy while in the foreign trades. Three of these ships are presently on one year charters to the Navy.

Ocean Shipholdings, Inc., supports the concept of establishing a revolving-type fund as a vehicle for providing the maritime industry with the means to construct, and place in operation, commercial vessels which could also be used by the U.S. government as military auxiliaries in time of war or national emergency. S. 1885 has the potential to enable the construction of new merchant vessels without impinging on any existing owners or operators of U.S. flag vessels. We see this as an important feature for the proposed "Build and Charter" program.

I will now address three often asked questions regarding the proposed "Build and Charter" program: (1) the appropriate role of the Maritime administration in the consultative process; (2) the existence of over-tonnaging in categories of vessels proposed to be constructed; and (3) the economic feasibility of chartering in light of specific limitations on markets, subsidy, and charter fees imposed by the House ligislation. I will attempt to answer these questions in that order.

The Maritime administration through its various functional offices has experienced personnel who can assist in: (1) the determination of foreign ship construction costs; (2) the analysis of the economic impact on other U.S. operators of introducing new tonnage into existing shipping market segments; (3) the soundness of companies bidding on the construction, purchase or charter of these ships; and (4) the specification and commercial impact of vessel design features required by the Navy for these ships to be considered useful military auxiliaries. I do not mean this to be an exhaustive list of the capabilities of the Maritime administration (MarAd); obviously, it is not. Rather, these are the specific areas in which we believe it will be able to assist the Navy in the administration of the House legislation.

We have carefully considered the process by which our company will be able to build and purchase (or charter) petroleum product tankers using the proposed fund. It is clear that any ships built to trade in foreign commerce will have to be compatible with the requirements of those trade routes. For certain types of vessels the installation of sealift enhancement features required by the Navy for military auxiliary vessels should be coordinated with MarAd to ensure that the vessels will retain their commercial utility. However, we urge the subcommittee to allow, in the final legislation, for the Secretary of the Navy to have the authority to make the final decisions concerning the design and types of vessels considered under this program.

The existence of over-tonnaging in the categories of vessels to be constructed, and the third question regarding economic feasibility are closely related.

It is a fact that, in the market for foreign trading tankers at this time, a U.S. flag vessel has an operating cost handicap compared to a foreign crewed vessel. This results primarily from crew cost differentials. However, this operating cost handicap can be overcome rather quickly through increases in the world market tanker charter rates.

I will now address the economic viability of tankers constructed under the proposed "Build and Charter" program. For the purposes of an example, I will use approximations of estimated actual costs to represent a simplified case. These costs typically differ between operators and for different types of vessels.

Let us assume that a 30,000 ton product tanker can be built in a foreign yard today for $20 million. The operating cost differential we will assume to be $2 million per year. If the foreign market could provide the owner with a guaranteed return of his $20 million investment, through a long term charter for the life of the vessel, a ship purchased from the proposed fund by a U.S. operator would have an operating cost handicap, in present value terms of approximately $18 million. I reached this conclusion by discounting, at 10 per cent per year, the $2 million operating cost differential for 25 years. To summarize, if the vessel in our example actually has a $20 million value to a foreign buyer, a vessel purchased from the proposed fund would have only an actual $2 million value.

Another way to view this, is to recognize that a private company interested in chartering a tanker constructed under the "Build and Charter" fund will not in the present market be able to replenish the full $20 million foreign equivalent cost to the fund. If this were possible, we would be seeing U.S. flag tankers constructed in foreign yards.

We must keep in mind that shipping markets are not static and continue to move through normal business cycles. The prudent investor in ships is aware of this cyclical aspect to the market and attempts to capitalize on these cycles. When the market for tankers improves, the charterer may be in a position to pay a higher charter rate for the vessel. For this reason, we fully expect that the Secretary of Navy, in administering the fund, will compare the charterer's offered rate to the Navy's forecast of the market for similar ships. If the Navy determines that the charterer's offer is insufficient to "adequately replenish the fund," but will enable the operator to employ the ship throughout the term of the charter, then I expect the Navy will limit the term of the charter accordingly, in order to reevaluate the market periodically.

Through this process, it is probable that a vessel constructed today would return to the fund its full foreign equivalent costs over the 25 year useful life. So you see that the fund has actually only taken the capital recovery risk off of the shipowner, but has taken the reward commensurate with that risk as well.

In the private sector, businessmen take a certain calculated risk and expect that the reward for taking that risk will somehow be related. Inherent in this risk/reward process is the mechanism which will cause charterers to compete for fund vessels.

In the process of evaluating offers for ships proposed to be built using the fund, we expect that the Navy will also take into consideration the savings it will realize by having one less vessel to maintain in the National Defense Reserve Fleet. This cost to the Navy is roughly $1 million per year which could cover 50 per cent of the operator's cost handicap in the foreign trade.

At this time I would like to address the requirements for the largest charterer of U.S. flag product tankers: the Navy's Military Sealift Command (MSC). Due to the presently depressed U.S. flag tanker industry, the MSC is having to depend on an increasingly obsolete pool of available tankers. Most of these ships are presently over 20 years old and were built with relatively fuel-inefficient steam turbine engines for their main propulsion. The commercial market will not support the construction of newer, more efficient tankers.

We urge the subcommittee to adopt an amendment that will allow flexibility on the part of the Navy to have vessels which are built under this program to be chartered to the Military Sealift Command. While these vessels are under charter to the Navy these vessels should be allowed to trade in the coastwise domestic trades.

In order to protect independent shippers and operators, we also urge the inclusion of an amendment that provides that while fund vessels are on charter to the Navy, and are carrying cargoes in the U.S. foreign trades, the minimum capital charter element be directly related to the owner's capital recovery costs. The operating cost element should be unrestricted to provide the Navy with the most competitive operating economies.

In order to protect the coastwise vessel operators, we would also suggest that the same amendment provide that while the vessel is in the coastwise trades, a mini-

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mum capital charter element would be established based upon the actual total cost of the vessel and the operating cost element would again remain unrestricted. This would provide the Navy with the further flexibility to trade the ship anywhere in its supply system while providing a strong incentive to use available tankers which can be offered at lower rates.

Also, we believe that Sec. 1408(3) should be amended to consider the exposure of an operator that may have rechartered the vessel in the commercial market. It is not reasonable to assume that commercial charters would allow the vessel to be withdrawn without costs. The charterer of a fund vessel may also have to make additional investments in ancillary equipment, hire and train personnel or otherwise enter into financial commitments directly tied to the successful operation of a fund vessel. U.S. laws presently make adequate provisions for the President to requisition U.S. ships.

Our final suggestion is that in determining the "foreign costs" equivalent, the Secretary of Transportation should use the lowest costs available to an independent operator from a recognized and qualified shipyard. The independent operator would not make a decision to purchase a vessel based on any composite price computation. Rather, he would use every incentive-type price program available in the foreign shipbuilding market.

Mr. Chairman, Ocean Shipholdings strongly supports the consept of a "Build and Charter" program outlined in the proposed legislation. We believe, with the incorporation of our recommendations that the "Build and Charter" program will benefit our military and will provide opportunities to further develop the U.S. Merchant Marine industry.

I appreciate the opportunity to appear before your subcommittee today to present Ocean Shipholding's views on this important legislation. I will be happy to answer any questions you members of the subcommittee might have. Thank you.

Senator STEVENS. Well, I appreciate those comments and we look forward to looking at the language you mentioned about the economic viability. I know that you have been personally very interested in support of this legislation, so we are pleased you have taken the time to come and give us your suggestions.

Mr. Shapiro, you are right about the package concept. Our language in the bill may be inarticulate, but we are going in the same direction, and we would be pleased to work with you in that regard. And your counsel very able in this area.

Mr. Thomson, I appreciate the fact that you are not taking just an outright opposition stand, in view of the obvious conflict that exists with regard to the proposal and your three tankers. On the other hand, I heard Mr. Pyatt state categorically today a desire that he had only expressed as a wish before. I think that your position has changed by these hearings more than anyone else's.

Perhaps that objective may be reached without regard to this legislation in the near future. I know the Navy has spoken to us about the tankers, in my other subcommittee anyway.

I have no questions about the comments you made, except to say that, again, we look forward to working with you and all others who are interested in the legislation. We are going to await the outcome of the House deliberation and see what happens to the proposal that is being brought out of the Senate Armed Services Committee, which is adverse to the use of the Mariner money that is earmarked in the Department of Defense appropriation bill for 1986.

Both of those actions I think have to be reacted to by the Senate before we would consider moving this bill. I do expect to see action by the House on one of the proposals, and we would like to have the interest expressed by the industry to the provision that is in the Armed Services bill.

I do not think it has been reported out yet. It is due out today or tomorrow, I assume that we will have to address that issue first, even before the House bill gets here.

But thank you all very much for your help in establishing a record concerning this. We will be back in touch with you when the time comes—we hope it will come—that we feel that we ought to attempt to move the bill out of Committee.

Thank you all very much.

[Whereupon, at 4:05 p.m., the subcommittee was adjourned.]

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ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF MICHAEL S. WASACZ, PRESIDENT AND CHIEF OPERATING OFFICER, MATSON NAVIGATION COMPANY, INC.

Mr. Chairman and Members of the Subcommittee: As President of Matson Navigation Company, Inc. ("Matson") I appreciate this opportunity to present Matson's views on S. 1832 and S. 1833.

Matson's operations as a common carrier of cargo are primarily between the United States Pacific coast ports and ports of the State of Hawaii. It is therefore vitally interested in the provisions of Section 1401(h) of S. 1832 and Section 1401(h)(2) of S. 1833 which would permit the Secretary of the Navy to charter or sell merchant vessels constructed under the section for operation in the coastwise or intercoastal trade, "if the Secretary finds that it is in the interest of national security to so charter or sell any such vessel." These restrictions on the chartering or selling of merchant vessels constructed under the section recognize that such vessels should be permitted to operate in the coastwise or intercoastal trades only under exceptional circumstances related to the national defense. The quoted language of the bills, however, would create a new and unacceptably vague standard because the term "in the interest of national security" is undefined. Further, the bills contain no provision affording notice and the right to be heard to existing coastwise or intercoastal operators.

Public Law 1981 of the 81st Congress (64 Stat. 2210) enacted December 27, 1950 provides for waiver of the navigation and vessel-inspection laws upon the request of the Secretary of Defense "to the extent deemed necessary in the interest of national defense by the Secretary of Defense." Public Law 891 has been in effect for 35 years, has been the subject of proceedings before the Secretary of Defense as to what he should deem necessary "in the interest of national defense," and provides a more meaningful standard than the vague language "in the interest of national security" in the bills.

It is recommended that Section 1401(h) of S. 1832 and Section 1401(h)(2) of S. 1833 be revised to read: "The Secretary shall not charter or sell to a citizen of the United States for documentation under the laws of the United States any merchant vessel constructed under this section for operation in the coastwise or intercoastal trade, unless the Secretary of Defense directs a waiver of compliance with this section to the extent he deems necessary in the interest of national defense, after affording notice and an opportunity to be heard to existing coastwise or intercoastal trade operators."

AMERICAN INSTITUTE OF MERCHANT SHIPPING,
Washington, DC, March 19, 1986.

Hon. TED STEVENS,
Chairman, Merchant Marine Subcommittee, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, DC.

Dear Mr. Chairman: The American Institute of Merchant Shipping (AIMS) is a national trade association representing 22 U.S.-flag shipping companies which own or operate approximately nine million deadweight tons of tankers, dry bulk carriers and other oceangoing vessels engaged in the domestic and international trades of the United States.

The purpose of this letter is to express AIMS views on the concept of "build and charter" in general and to provide specific comments on S. 1885. We would appreciate this letter being made part of the March 20, 1986 official hearing record of S. 1885.

AIMS can support the concept of a build and charter Program (Program) as a vehicle for providing militarily useful commercial vessels for use by our government as a naval and military auxiliary in time of war or national emergency. A properly

drafted Program would supplement the reserve fleet. It would provide operating vessels immediately available to the military and a reserve of seagoing personnel which could be used to operate both build and charter vessels as well as vessels to be activated from the reserve fleet in times of national emergencies. Since an adequate defense capability is no longer available as a cheap by-product of our commercial fleet, then government programs such as build and charter are a way to supplement our commercial fleet. To this effect, any such program should be crafted to provide vessels which have military utility and which add to, rather than substitute for, existing commercial vessels. It is neither appropriate nor good public policy that Federal funds be used to build commercial vessels that compete with and eventually displace vessels constructed without such support. Furthermore, the program should not reward or penalize any individual operator in any trade, foreign or protected.

Before giving you our comments on specific sections of S. 1885 listed below are eight points of principle which should apply to any build and charter program:

1. The Program should only be applicable to vessels approved by the Department of Defense as being: (a) militarily useful; and, (b) of a type in short supply. (Excess tonnage of any class or type vessel should be avoided.) A study of the type that the Commission on Merchant Marine and Defense was charged with conducting in October of 1984 should be completed prior to implementing the Program.

2. All vessels should be of a commercial design with military features added. The design should be developed by both commercial interests and the military so that the commercial and military features blend together without conflict. The design should incorporate the latest concepts of equipment and machinery to achieve optimum operating economics, including lowest fuel costs and minimum manning levels.

3. Program vessels must not be allowed in the domestic trades unless the President declares that a state of national emergency exists and they should be withdrawn from the domestic trades as soon as the emergency terminates. Domestic trades include our coastal, intercoastal, Great Lakes, and non-contiguous trades and the trade of government impelled cargoes. Failure to include a strong enforceable domestic trade exclusion and allowing vessels in the domestic trade would further depress the domestic market and cause further devastation for owners which, in turn, would lead to bankruptcies and the loss of existing militarily suitable tonnage.

4. The Program should be limited to the chartering of these government owned vessels—sale should be prohibited. This would provide the minimum disruption in the marketplace and the maximum assurance that a vessel would remain in operation during its useful life, i.e., not be laid up. Vessels can easily be re-chartered to another operator is the first charterer has difficulty in keeping the vessel in operation. Re-sale is much more difficult.

5. There should be a very concise and easily understood bidding process open to all operators.

6. No direct subsidies should be granted to charterers of Program vessels, nor should they be replacement for existing subsidized vessels. Each bidder should calculate his proposed charter rate so to offset his higher actual costs, i.e., wages, insurance, P&I, etc. vis-a-vis his foreign competitor.

7. The government should recognize that the Program shall not be self-funding and start-up should be contingent on a commitment by the government to provide future appropriations. Based on today's charter rates, revenues in the liquid bulk market would not cover U.S. operating costs and full capital recovery. In short, the fund would not be self-replenishing.

8. An offer of Program vessels at rates based on notional foreign building costs would not bring bidders forward. Such rates are presently available commercially as any owner can flag a foreign-built ship in the U.S. and even lower rates are available on reflagged used foreign built tonnage. Acceptance of the concept of a "subsidized" bareboat charter rate, i.e., one below full cost recovery of even the notional foreign building costs to compensate for higher capital and operating costs would be needed today if the proposed Program is to succeed.

On the other hand, such a policy would serve to undercut the viability of U.S.-flag Construction Differential Subsidy (CDS)/Operating Differential Subsidy (ODS) built vessels currently in services. Given the low time charter rates and spot rates presently available, the existing U.S.-flag CDS/ODS vessels are struggling to exist.

AIMS supports S. 1885 with several reservations which are detailed in the following comments:

1. Section 1401(b)(2)(C)—We assume that "at least 50 per centum of the cost of all machinery etc.," refers to 50 per centum of the total cost and not 50 per centum of each individual items so that important components such as a diesel propulsion unit would not be excluded.

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2. Section 1402 states at the Secretary shall not sell the vessel at less than foreign building costs. Sections 1402 and 1405 requires that the charter hire must be at least sufficient to amortize the debt as if the vessel had been built in a foreign shipyard. In the liquid bulk trades such a rate added to the higher operating costs incurred on a U.S.-flag vessel would be non-competitive. A competitive charter hire rate in today's market, would not enable the government to recoup the foreign construction cost element of the monies spent to finance Program vessels much less replenish the Revolving Fund.

3. Section 1402(a)—Although "citizen of the United States" is not defined, we assume that Section 2 of the Merchant Marine Act of 1916 applies to Program vessels being offered at a "subsidized price."

4. Section 1402(b)—The Program should be limited to the chartering of these government owned vessels—sale should be prohibited. This would provide the minimum disruption in the marketplace and the maximum assurance that a vessel would remain in operation during its useful life, i.e., not be laid up (see Item 4, Page 2). This Section and all other references to sale should be deleted.

5. Section 1402(c)—See Section 1402(b) above. However, for use as one element in evaluating charter rates, the Secretary of Transportation, on an as needed basis, should compute appropriate foreign building costs. This should be done in concert with industry. Once Computed, the numbers should be published.

6. Section 1405(c)(1)—"Replenish adequately," is such a subjective term as to be useless and confusing at best, especially when, in today's market, the government will not recoup the monies it spends to build a vessel. If Section 1405(c)(1) is not deleted, the Program will not succeed, and if deleted will result in non-replenishment of the revolving fund and set in place a form of indirect operating subsidy contrary to Section 1404(a). Today's foreign trade commercial market will not support liquid bulk vessels built at the lowest foreign building cost but operated at U.S.-flag costs.

7. Section 1405(e)—The Secretary "shall" not "may" promulgate such regulations, etc. The charter parties required to implement this statute should be spelled out in detail in a set of regulations. To a considerable degree, the success of the build and charter Program will depend, among other factors, on reasonable and equitable charter arrangements.

8. Section 1406(a) and (b)—This Section should be deleted in its entirety. The Secretary's excess profit tax clause would be unacceptable to any "prudent business man" who, by virtue of a firm bareboat charter, is taking on debt in the form of a contingent liability. Capping profits at 10%, with 50% sharing over that figure, would go a long way toward guaranteeing that the charterer would not make a fair return on his "investment," and probably no return at all. The shipping market is a highly volatile and cyclical market and profitable rates must not be capped, otherwise losses suffered during down-turns could not be covered and the venture would most likely fail.

Charterers' profits and losses should be of no concern to the government. Government's concern should be prompt receipt of agreed upon charter payments, continual operation of the vessel, and adequate maintenance of the vessel, including defense features. If the Secretary is concerned that a firming market could result in "excess profits," the Secretary could reduce the time period of the charter so as to, by competitive bidding, reset the rates more frequently during the life of the vessel. Charter hire bids would almost certainly be higher in the absence of Section 1406 than if it is retained. Adoption of a normal commercial charter arrangement would avoid the administrative costs which would otherwise be involved in eforcing in enforcing the provisions of Section 1406.

9. Section 1408(3)—While the government has the right and obligation to requisition Program vessels in time of national emergency, the charterer has the right to be protected from real losses due to such actions. Therefore, strike the language "without cost to the United States" (from line 13, page 8) and deal with determination of losses in the charter party.

10. Section 1409(a)—Insert a period after the word "completed" on line 24, page 8 and, strike through the remainder of this Section. These vessels should add to, rather than substitute for, existing commercial vessels.

11. Section 1409(b)—Strike proposed language and substitute "Any vessel construction under this Section shall not be allowed in the domestic trades, i.e., coastal, intercoastal, Great Lakes and non-contiguous trades, or the trade of government impelled cargoes, unless the President declares that a state of national emergency exists and, they shall be withdrawn from such trades as soon as the emergency terminates."

12. Section 1410 should be deleted. The Commission on Merchant Marine and Defense (the Bennett Commission) will make the necessary in-depth studies and reports required to gain a full understanding of our present and future military and commercial needs. The Maritime Administrator, as co-chairman of the Bennett Commission, can ensure that any studies necessary to address maritime policy matters are made.

Again, Mr. Chairman and members of the Subcommittee, thank you for the opportunity to submit comments for the record. If we may be of any further assistance, please feel free to contract us.

Respectfully submitted,

THOMAS J. LENGYEL, *President.*

NATIONAL MARINE ENGINEERS' BENEFICIAL ASSOCIATION,
Washington, DC, March 11, 1986.

Hon. TED STEVENS,
Chairman, Merchant Marine Subcommittee, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, DC.

DEAR SENATOR STEVENS: Unfortunately, I will not be able to appear in person to testify on S. 1885 on March 20th, but I would like you to have my views on this revised bill and would ask that they be included in the hearing record.

As you know, I expressed my views on the build-and-charter proposal on November 15, 1985 when it was still embodied in S. 1832 and S. 1833. I said then, and I would emphasize again, that I support wholeheartedly the concept of build-and-charter. It will create an operating fleet with trained crews, not a mothball fleet with nobody left to operate it if these vessels are ever broken out in war.

However, as I also said then, it is not enough to create such a fleet. Its vessels must be commercially viable lest they become an intolerable drain on the Treasury. Above all, they must have cargo, and without policies to create a new source of cargo for these vessles, we will simply have more ships trying to carry the same amount of cargo and that would be a disaster for our present fleet.

This revised bill does little to allay my concerns on these two fundamental points: commercially-viable vessels and cargo to go on them. The fact that solutions to these concerns are absent only strenthens my long-held view that plans to help our fleet must be comprehensive, not piecemeal—no matter how well-intentioned a partial solution may be.

Technically, in its drafting, S. 1885 is an improvement over its predecessors, although I would stress several points again that I made in November:

Important terms such as "citizen" are left undefined;

Operators of these build-and-charter vessels may not receive ODS for these vessels (I believe they should); and,

Vessels built under this program are excluded from the Trans-Pacific and Trans-Atlantic general dry cargo liner trades (I do not believe they should be excluded).

I recognize, however, that despite the points I have raised, this program may go forward. If this is the case, I would urge that the Committee consider two additional changes to the bill that could be incorporated relatively simply.

First, I would recommend that a portion of the build-and-charter funds—such as one-fourth—be set aside to promote the building of passenger cruise vessels in U.S. yards for the Jones Act trades. While these vessels would be of obvious military utility in certain scenarios, funding a portion of their construction costs would be the quickest and surest way to establish a U.S.-built, U.S.-flag domestic cruise industry. This is one area of the maritime industry wher the "cargo" is there but not the vessels. There clearly is substantial interest, among investors as well as operators, in building vessels in U.S. yards for this trade, but most of the proposals have come close but then failed due to their inability to obtain full financing. Because the Jones Act trades are a special market where U.S.-built vessels would only compete with other U.S.-built vessels, the amount of Federal financing would not have to be the dominant percentage. I do not have a formula for what percentage should be paid, but I am certain that an equitable, cost-effective percentage of Federal financing, when added to private investment interest that is already there, would be enough to put these projects over the top and get them started.

The Jones Act cruise ship industry offers great potential for U.S. yards, for the U.S. steel that would go into these vessels, for U.S. workers here at home, and for U.S. mariners. A portion of the funds in your program, so directed, could get this industry started. It would enable our industry to join together to build a uniquely U.S. segment of the world cruise trade.

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My second suggested change concerns Section 1410 of S. 1885 which calls for a study of the build-and-charter program in this proposal as well as other promotional programs within the jurisdiction of MarAd to "determine their potential application to the coastwise trades. . . ."

I would strongly urge that this study be broadened to include a comprehensive look at the entire Jones Act and ways in which it might be strengthened and changed—if necessary—to build up our fleet. This study could include everything called for in Section 1410, except that I believe that the study should be done by an independent contract group reporting directly to the Congress but charged to seek out the views of all segments of our industry. The Jones Act is one of the last remaining bulwarks of our industry. As I have said elsewhere, I do not believe every one of its words is necessarily chiseled forever in stone, but, if changes are to be made, they should be fair, balanced, and above all, comprehensive.

Thank you for providing me this opportunity to express my views. I would be happy to discuss the points I have made with you or the Committee at anytime in more detail.

Sincerely yours,

C.E. DEFRIES, *President.*

INTERNATIONAL ORGANIZATION OF MASTERS, MATES & PILOTS,
Washington, DC, March 19, 1986.

Hon. TED STEVENS,
Chairman, Subcommittee on Merchant Marine, Committee on Commerce, Science, and Transportation, Hart Senate Office Building, Washington, DC.

DEAR MR. CHAIRMAN: I am writting in response to your invitation to testify on S. 1885, a bill "to authorize the establishment of a Military Auxiliary Revolving Fund within the Treasury of the United States." I regret that prior Union business commitments preclude my appearing before your Subcommittee, and I request that the following comments submitted on behalf of the International Organization of Masters, Mates and Pilots, ILA, AFL-CIO, be included in the Subcommittee's hearing record on S. 1885.

The Masters, Mates and Pilots has long advocated the creation and implementation of a build and charter program. At our 1982 Biennial Convention, the delegates representing our Offshore and American Radio Association divisions unanimously voted to place before our membership a referendum entitled "Measures to Strengthen and Revitalize the United States Merchant Marine." This measure, adopted by our Offshore and ARA membership groups, called for the establishment of a build and charter program with a revolving fund. It reflects our Union's belief that we need American-built, American-flag ships for our economic well-being and our national defense.

The MM&P's support for a build and charter program is still strong. S. 1885, patterned after the successful Mariner Program of the 1950's, would create a Federal revolving fund to finance the construction of militarily-useful merchant vessels in United States shipyards. These vessels would be leased or chartered to American commercial operators for participation in the U.S.-foreign trades. The proceeds from such transactions would be deposited in the revolving fund to finance the domestic construction of additional vessels.

Due to your efforts, Mr. Chairman, and the efforts of your Subcommittee, $852 million in unobligated Department of Navy funds is earmarked for the proposed build and charter program. With authorizing legislation, a build and charter program will be established and funded to create much needed business for American shipyards; to increase the number of modern and efficient vessels operating under the American-flag and to enhance the overall seapower posture of the United States.

As this Subcommittee works to formulate and authorize a build and charter program there are various suggestions that we believe will result in a program that benefits both domestic shipbuilders and American-flag vessel operators, and which will generate new employment opportunities for American Workers in the shipboard, shipyard and longshore segments of our industry.

First, we believe that any vessels built under this program should be economically viable as well as militarily useful. In order to better accomplish this objective, the Secretary of Transportation or the Maritime Administrator should play an equal role in the vessel selection process with the Secretary of the Navy. In so doing, the economic realities of the commercial maritime industry would be reflected in the decision-making process. If the vessels built under build and charter cannot compete

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commericially, we will have spent money to create a mothball fleet and have done nothing to expand the number of active, trained seafaring personnel needed to man these vessels in time of war or national emergency.

Secondly, the build and charter program should be as broad in scope as possible in order to generate maximum commercial maritime work consistent with present and future national defense considerations. Build and charter can serve as the vehicle which enables the maritime industry to expand into new and underdeveloped markets, although the prohibition against operating cargo vessels built under this program in the domestic trade should be retained. Existing American operators of Jones Act vessels have consistently provided American business and consumers with an efficient and economic means of transportating commodities between American ports.

On the other hand, the legislation should extend build and charter to the construction of passenger vessels for operation in the domestic trade. Over the past few years, there has been an ever increasing amount of attention devoted to ways to increase the number of American-flag cruise vessels. Numerous American entrepreneurs and domestic shipyards have worked diligently to finalize their financing arrangements in order to build and rebuild cruise vessels in this country. Unfortunately, for various reasons, including the uncertainty in financial circles over what if any changes in existing law Congress may make, full financing has not yet been available to prospective American cruise vessel operators.

I believe the build and charter program can end this uncertainty and help create a segment of the American maritime industry which is virtually non-existent. The construction of economically viable cruise vessels will provide tremendous economic and defense benefits.

We are of course aware that allowance will have to be made in the charter agreement to ensure that existing or future domestic operators of American-built cruise vessels—built without build and charter funds—will not be adversely affected. It is our objective to have build and charter increase the number of operators and the number of economically viable, militarily useful cruise vessels, not to advocate a program which grants any operators an unfair competitive advantage.

Thirdly, the build and charter program should reflect the fact that the most important component of a national maritime policy and the key element which must be present if we are to achieve the maritime strength this nation must have is best summed up in one word: cargo! We should, for example, actively pursue the negotiation of bilateral cargo sharing agreements with America's trading partners. The so-called free trade policy expressed by this Administration and others before it is little more than an excuse to do nothing in response to the trade and maritime policies of most other nations. As we stand alone playing by one set of rules, our trading partners, allies and others continue to capture greater shares of our commerce for their flag vessels through cargo reservation policies, tax and other financial incentives, or a strong commitment to use national flag ships.

Constructing vessels under a build and charter program does not alone solve the problems facing our industry. Nor does it alone make us totally competitive in the international shipping arena, provide an immediate increase in the number of American-flag merchant vessels, or generate urgently needed employment for American merchant mariners. Consequently, we believe the build and charter authorizing legislation should further expand the private industry's ability to acquire new, modern commercial vessels at competitive prices.

Specifically, American operators should be allowed to build or acquire foreign vessels for operation under the American-flag with immediate eligibility to carry U.S. government preference cargoes. Taken together, build and charter can provide work for domestic shipyards and foreign building can provide a boost for American operators and seafaring labor.

Allowing foreign-built vessels to carry preference cargoes without waiting three years after documentation under the United States-flag will accelerate the creation of a modern American fleet. Such reflagged vessels should be limited to newly-built ships, those which are three years of age or newer. These vessels can also contribute to the ongoing effort in our industry to reduce costs and increase the efficient transportation of preference cargoes.

These changes should be undertaken in such a manner so as to treat American operators equally while benefitting the industry as a whole. Your efforts and the efforts of the Subcommittee on Merchant Marine in advancing build and charter may set our industry on its road to recovery. I assure you that the Masters, Mates and Pilots stands ready to work with you to achieve a build and charter program

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which contributes to the revitalization of the American shipbuilding and ship operation industries.

Sincerely,

Capt. ROBERT J. LOWEN,
International President.

STATEMENT OF AMERICAN AUTOMAR, INC.

SECTION 1401

Section 1401 defines the source of funds for the program and outlines a general set of construction requirements and conditions. As such, it is the "enabling" section of the legislation. In conjunction with making a U.S. building program a reality, Automar believes the Navy and MarAd should define priorities for the types of vessels to be built under the S. 1885. Such priorities have been employed in MarAd's purchase of vessels for the Reserve Fleet and Automar has always supported the policy as a vehicle for achieving the optimum balance in sealift assets. Without such a mechanism in S. 1885, there is a good chance that the legislation may develop into a "CCF" program for container operators, thereby insuring that the U.S. flag fleet remains in a "steady state", with regard to cargo handling capability. In addition, with the advent of jumbo container ships, a container carrier program will probably lead to an absolute reduction in fleet size.

While there is an acknowledged place for container ships in sealift operations, Automar feels the fleet is badly in need of operating assets which offer a wider range of cargo handling capability. We feel MarAd's purchase policy under the Reserve Fleet RFPs, as well as MSC's chartering practices over the past several years, have acknowledged that military planners recognize the fleet has become too container-oriented to the possible detriment of contingency sealift capability. We would suggest, therefore, that the Navy and MarAd jointly develop a list of high priority sealift assets which, assuming all other factors, were equal, would be first chosen under the Build and Charter program.

Within this list of high priority assets we would include:

(1) Pure car/truck carriers.

(2) Handy size product tankers.

(3) Heavylift/project ships.

Such an approach would add balance to the U.S. fleet's cargo handling capability, as well as enhance and diversify U.S. shipbuilding capability.

SECTION 1402

This Section outlines the charter or purchase options open to the Government under the program. Although it is easy to see that the construction of product tankers or standard container ships would result in bids from any number of companies operating in such trades, there is some question as to how the mechanics of the legislation would work for the project type assets outlined above. For example, should the Navy/MarAd decide it was desirable to build one or more PCTCs, what size, speed, or configuration would be chosen. As you know, these and other specialized project ships are generally constructed for certain markets/cargoes. The "blind" construction of such vessels more often than not would result in turning out ships marginally suited for a large number of trades and ideally suited for none. Such an approach would probably lead to inefficiencies and ultimately higher costs. As an alternative for the higher priority vessels, we would suggest the Navy and MarAd work more closely with the private sector owners, operators and users in developing program parameters and vessel specifications. Such an approach would not reduce the program's competition or increase cost to the Government, but would result in increased commercial economies and ultimately lower Government outlays.

For example, the Navy could announce its intention to build and charter/sell a PCTC. The private sector would then be requested to submit bids for charter hire and/or purchase prices for specific types of PCTCs for which their individual companies had prospective employment. From these bids, the Government could select the most economic proposals and best suited vessel design to be bid out to U.S. shipyards. Such an approach would result in the best economic and commercial "fit" for the project type vessels.

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SECTION 1407

This Section in part provides for termination of the charter on national security or defense grounds. This somewhat brief and, as yet undefined mechanism, could be structured and expanded to the benefit of the Navy without unnecessary harm to commercial operators.

In the first instance, the charter need not be terminated under the conditions noted. As with the Military Sealift Command's Ready Reserve Fleet requirement under the common carriage RFP, charterers or owners of Build and Charter vessels could be required under certain conditions to make their assets available when and where necessary to the Navy at negotiated charter hire rates. This would provide the Navy with a "ready" ship fully manned. Such an approach is clearly preferable to the operator turning the ship back to the Navy and simply walking away.

Second, the charter could contain a provision mutually agreeable to the Navy and the charterer/owner stating that the vessel could be periodically employed in Naval exercises. Such a mechanism would provide valuable manpower and logistics training for both the Navy and the commercial operator.

SECTION 1409

Section 1409 places operating restrictions on the geographic areas in which chartered vessels can operate. Automar believes this Section is extremely near-sighted and recognizes only the preferences of existing container liner operators to the detriment of developing a well-rounded U.S. flag fleet. Section 1409 not only eliminates new carriers from entering the program in the two single largest U.S. trade routes, it also serves to reserve and maintain monies for replacement of container vessels, the most abundant vessel type in the U.S. fleet.

We believe this Section of the Bill is contrary to the spirit of the legislation and as such, will ultimately work to the detriment of the Navy and MarAd's objectives. Nevertheless, recognizing the interests and influence of the established container operators, Automar believes that section 1409 can be amended to minimize its negative impact by inserting a new subsection. This subsection would qualify the restriction so that it applied only to container vessels. Project ships such as PCTCs, heavy-lifts, Ro-Ros, tankers and others named by the Navy, would be excluded from the restrictions of Section 1409 completely. Without such a qualification, there is little chance the Navy would achieve any significant fleet diversification.

JAPAN'S YARD ORDERS MAY HIT 7-YEAR LOW

(By A.E. Cullison)

TOKYO.—Foreign orders for newbuildings during the current fiscal year, which ends March 31, are expected to drop to a seven-year low, the Japan Ship Exporters' Association said.

The association disclosed that total orders from abroad for new ships probably will sink beneath 3,000,000 gross tons. They pointed out that vessels under construction in Japanese yards or on order at the end of last month amounted to only 6.8 million gross tons (265 ships).

It was reported that in February Japan's shipbuilders received orders from overseas for just six vessels totaling 125,150 gross tons; these orders, the association disclosed, were valued at around $96 million, down by 49.6% compared with the same month of last year.

Association officials noted that three of the ships ordered by owners outside Japan in February were covered by contracts denominated in dollars.

This situation, they emphasized, reflects the recent dramatic appreciation of the yen's value against the U.S. dollar. If this sharp appreciation of Japan's currency continues, the executives stressed, large foreign exchange risks will affect most if not all foreign order placements. It is an unhappy situation for Japanese yards.

In addition, it was noted that those foreign shipowners who normally would place orders denominated in yen will find themselves in trouble when they have to purchase the Japanese currency on foreign exchanges to make their payments.

Meanwhile, Kazuo Maeda, president of the Shipbuilders' Association of Japan, told newsmen the industry's leaders are giving serious consideration to the formation of an anti-recession cartel.

Such a cartel, given Japanese government approval, would work to curtail operations of all association members in order to permit the yards to survive the current business slump.

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He advised that the association plans to establish a panel of experts to study the various problems that would have to be met in setting up an industry-wide cartel arrangement. It is presumed that the cartel would cover fiscal years 1987 and 1988.

As matters now stand, Mr. Maeda reminded, the association would have to receive the authorization of the Fair Trade Commission before a cartel could be organized. This authorization is likely to be applied for this summer, he said.

Mr. Maeda, who concurrently is president of Mitsui Engineering and Shipbuilding Co., informed the press that a cartel probably would reduce the industry's yearly ship construction to between 3,000,000 and 3,200,000 tons in terms of the compensated gross registered tonnage.

The present guideline laid down for the industry by authorities of the Ministry of Transport is 4,000,000 gross tons annually. The cgrt. is a measure of a shipbuilder's construction volume.

FARRELL LINES, INC.,
New York, NY, March 25, 1986.

Mr. JOHN HARDY,
Democrat Merchant Marine and Tourism Counsel,
Washington, DC.

DEAR JOHN: At the Senate Sub-Committee Hearing on S-1885, "A Build & Charter Program", you asked me to comment on several questions. Attached hereto are copies of the questions, with my answers on behalf of Farrell Lines Inc. annexed thereto. I hope they will be helpful.

I am sorry that Senator Inouye was unable to be in attendance, but trust you will brief him on all that transpired.

Sincerely,

GEORGE F. LOWMAN, *Chairman.*

Enclosure.

Question. If S. 1885 is enacted do you intend to build any ships under the program; and if so, how many and what type?

Answer. If S-1885 is enacted, changed, and modified to include the suggestions set forth in my remarks, a copy of which is attached, Farrell Lines would be prepared: To build and/or charter up to six ships—such ships to include combination Container/Break Bulk, and RO/RO characteristics, with a capacity of 41300 TEUs, 250,000 cu ft. and self-sustaining.

Question. The Assistant Secretary of the Navy has testified that the two-step procurement process in the legislation will not work:

Step 1—Competition for construction of a ship;

Step 2—Competition for chartering the ship.

He went on to say that if a build and charter program were instituted, it should be designed so that shipbuilders and ship operators present proposals for construction and charter operation. This would prevent construction of ships for which there are no markets.

What are your views?

Answer. The Assistant Secretary of the Navy is correct that the two-step procurement process will not work.

As stated in my remarks, to be competitive, the ships must be designed and built for the particular carriers and trades in which they will operate. Plans for such construction should be developed by the selected carrier and modified as mutually agreed with the Navy to adjust to its military needs.

Question. At the Subcommittee's earlier hearing on build and charter, at least two witnesses (Frank Drozak, Gene DeFries) said that for a build and charter program to be successful, there must also be some sort of additional cargo enhancement policy.

Do you agree?

Answer. A cargo enhancement program would be desirable and helpful, but it would not be a necessity in our view.

Question. S. 1885 restricts any vessel built under the "build and charter" program from operating in the trans-Pacific or trans-Atlantic general dry cargo liner service, except as a replacement vessel.

Inasmuch as the trans-Atlantic and trans-Pacific are two of our busiest trades, is this restriction at cross purposes with the intent of the bill to build "commercially viable" vessels?

Is there an inconsistency between this restriction and other proposals to remove trade route restrictions from vessels receiving ODS?

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Answer. See my remarks to the Sub-Committee, the restriction against operations in the trans-Pacific and/or trans-Atlantic would be at cross-purposes with the intent to build "commercially viable" vessels, as far as Farrell is concerned.

The restriction would be inconsistent with the proposal to remove trade route restrictions from vessels receiving ODS.

Question. Do you support build and charter legislation irrespective of whether build-foreign legislation is enacted?

Answer. Farrell Lines does not support build and charter legislation without build/charter foreign legislation.

Question. One witness (APEX Marine) this morning will state that it is his understanding that under S. 1885, "the Navy will build the vessels and design them; and therefore any commercial charterer or purchasers will presumably be buying a shelf item from the Navy."

At our earlier hearing, however, the same witness said that "supervision of and actual choice of a particular vessel's design should be reserved for the industry's private sector, who are knowledgeable about the commerical requirements needed to ensure the competitiveness of each vessel in its eventual trade."

Another witness (Shipbuilders) will testify that it is his understanding that the Navy would engage the Maritime Administration as its procuring and chartering agent.

What are your views about the proper division of authority with respect to the choice of the type of vessel, its design, etc.; and should S. 1885 spell out in more detail who has the say about what, as among the Department of the Navy, MARAD, and prospective charterers or purchasers?

Answer. As I have previously stated, to be competitive, the American Merchant Marine needs the best designed, and constructed ships obtainable. We cannot compete with makershift equipment.

A "shelf item from the Navy" would be "makeshift" and unacceptable. Notwithstanding the above, mutually agreed modifications and/or changes (from a carrier designed ship) could be worked out with the Navy.

Question. At the Subcommittee's earlier hearings one witness (APEX Marine) recommended that in no event should the annual charter hire be less than 16½ percent of the foreign cost of constructing the vessel in a foreign shipyard. In other words, the bill should establish a floor.

The reasoning behind that recommendation is as follows.

The 16½ percent is intended to represent a 4 percent annual depreciation charge and a 12½ percent annual interest. When a vessel is chartered to an operator, it amounts in effect to the loan of the capital asset and the bareboat charter hire should at least reflect the annual depreciation on the asset, plus an interest factor for the loan of its capital value. The 4 percent represents annual depreciation based on a 25-year life and 12½ percent is an estimate of the long-term interest rate which would be applicable under Title XI financing or similar financing.

Do you have any thougints on a floor, and this particular recommendation?

Answer. Farrell Lines concurs that S-1885 should establish a floor for annual charter hire based on the foreign cost of construction in a foreign shipyard.

However, we believe the rate should be 12% to include 4% depreciation, 7% interest, and 1% insurance—based on present interest rates.

A standard could be readily established to determine the charter rate at the time of delivery based on the rates prevailing at that time.

Question. Last December, the House/Senate conferees on the Continuing Resolution to fund DOD, expressed their intent that legislation authorizing a build and charter program include authority for the Secretary of the Navy to charter commercially the 13 ships recently acquired for the Sealift program.

Should S. 1885 be amended to provide that authority for the Secretary of Navy?

Answer. When the Government purchases ships for the Sealift Program, it sets up a procedure to remove technically obsolete Merchant Marine tonnage from the industry, and to acquire militarily useful tonnage for the Navy available in times of emergency.

Accordingly, S. 1885 should not be amended to permit the charter of such vessels.

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